ADMINISTRATIVE REFORMS COMMISSION

REPORT

OF THE

WORKING GROUP

ON

Company Law Administration

ADMINISTRATIVE REFORMS COMMISSION

WORKING GROUP ON COMPANY LAW ADMINISTRATION

Chairman :

Shri D. L. Mazumdar

Members :

Shri Kali Mukherjee

Dr. R. K. Hazari.

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CHAPTER I

INTRODUCTORY

In its report submitted to the Administrative Reforms Commission on the 15th April, 1967, the Study Team on Economic Administration headed by Shri C. H. Bhabha, had briefly touched upon the role of Company Law Administration, but it was mainly concerned with the wider issues of economic policy centering round the principal economic controls and the licensing of industries including the regulation of foreign investments. The Administrative Reforms Commission, therefore, considered it necessary to sponsor a depth study on several major issues relating to the corporate sector, with particular reference to the inter-relationship between the financial institutions and the working of joint stock companies and the factors which had a close bearing on the effective administration of the Companies Act and the fulfilment of the aims and objects underlying it. After a preliminary discussion of the scope and purpose of the proposed study with Shri D. L. Mazumdar, formerly Secretary to the Government of India in the Department of Company Law Administration, the Administrative Reforms Commission decided to set up a Working Group for this purpose. The constitution of the Working Group as announced on August 11, 1967, was as follows :—

1.	Shri D. L. Mazumdar, I.C.S. (Retd.), Formerly Secretary to the Government of India, Department of Company Law Administration	Chairman.
2.	Shri Kali Mukherjee, 177/B, Acharya Jagdish Bose Road, Calcutta-12	Member.
3.	Dr. R. K. Hazari, Professor of Industrial Economics, University of Bombay, Bombay	Member.
4.	Shri M. V. Venkataraman, Chairman, Simpson Group of Companies, in Madras, 2, Doraiswami Road, Madras-17	Member.
5.	Shri H. P. Nanda, President, Escorts Ltd., 12, Jor Bagh, New Delhi-3	Member.
6.	Shri P. B. Menon, Regional Director, Eastern Region, Company Law Board, Narayani Building, 27, Brabourne Road, Calcutta	Member.
7.	Shri S. Venkataraman, Director of Inspection and Investigation, Department of Company Affairs, New Delhi	Member-Secretary.

1.2. The terms of reference laid down for the Working Group included the following items :—

(i) to examine the organisational set-up of the Department of Company Affairs with a view to assessing its suitability for securing speedy despatch of business and for enforcing the provisions of the Company Law;

(ii) to examine whether the administrative machinery is adequate for preventing malpractices in company management;

(iii) to examine whether the procedural requirements of the Companies Act do help in the achievement of the socio-economic objectives;

(iv) to make suggestions for the elimination of irksome and avoidable procedural requirements which unduly abridge the area of managerial initiative and discretion;

(v) to examine whether the provisions of the Company Law relating to the private and public companies discriminate in favour of either of the categories and if so, whether this discrimination is justified in the interest of the economic development. The Group may also suggest rational principles for categorisation of the companies in the light of the country's socio-economic objectives and the requirements of the economic growth;

(vi) to examine whether the provisions of the Company Law relating to inter-corporate investments and other financial restrictions are suitably designed to secure wide dispersal of ownership and avoidance of concentration of economic power and to consider the extent to which they have been effective;

(vii) to examine whether the provisions of the Company Law relating to the remuneration of Manager, Managing Agents, Managing Directors, etc., follow any consistent and clearly defined income policy;

(viii) to examine if there are any clearly defined criteria guiding the extensive exercise of administrative discretion vested in the Government under the Companies Act;

(ix) to examine whether there is adequate institutional arrangement to ensure co-ordination and integration of the financing policies of Government and quasi-Government institutions with the objects underlying the regulatory measures pertaining to the corporate sector; and

(x) to consider any other aspects of the administration of Company Law that may have a significant bearing on the achievement of the aims and objects of the Law.

1.3. Having regard to the nature of the problems referred to the Working Group and the very limited time at its disposal, it was decided not to issue any formal questionnaire to elicit views on the terms of reference. It was felt that it would be a time-saving and more fruitful procedure to address a few selected individuals and representatives of business and professional associations, who by reason of their personal knowledge and experience could be expected to throw light on many of the problems included in the Working Group's terms of reference, and to help in the assessment of administrative performance in this area. Accordingly, comments were invited from a number of selected individuals on the issues referred to the Working Group.

1.4. A list of persons who responded to the invitation of the Working Group is given at Annexure 'A'. A few memoranda were also received from a number of leading trade associations like the Federation of Indian Chambers of Commerce and Industry; the Associated Chambers of Commerce and Industries; the Shareholders' Associations; the Stock Exchanges; the Institute of Chartered Accountants of India, etc.

1.5. The Working Group also interviewed a number of persons representing a cross-section of those associated with trade, industry, the professions of accountancy, solicitors, bankers and also a few Members of Parliament, etc. These interviews were held at Bombay, Madras, Calcutta and New Delhi. A list of those individuals and organisations is given at Annexure 'B'.

1.6. Background papers on a number of topics were prepared by some Members of the Working Group and the Research Staff of the Company Law Department. In addition, a few case studies were also undertaken. The Working Group is grateful to these members and the officers concerned in the Department of Company Affairs for their help and assistance.

1.7. Between October, 1967 and April, 1968, the Working Group held eight meetings—one each at Bombay, Madras and Calcutta and five at New Delhi spread over a period of about 24 days. The Working Group regrets that it was not possible to hold these meetings at shorter intervals in view of the preoccupations of some of its members both within the country and outside it.

1.8. The study of the voluminous evidence collected by the Working Group and its analysis entailed a heavy burden on the very limited staff strength at the disposal of the Group. The Member-Secretary of the Group had to carry on his work in

addition to his own duties as an officer of the Department of Company Affairs, Government of India, but towards the end of its labours he received some part-time assistance from Dr. G. Balakrishnan, Senior Research Officer, Research and Statistics Division, Department of Company Affairs, Shri S. S. Trehan, Senior Analyst of the Administrative Reforms Commission was attached to the Member-Secretary from the middle of November and was of much help in organising the meetings of the Group and preparing their reports. The Group is grateful to these officers for their assistance. The Group would also like to place on record its appreciation of the hard work put in by its Secretarial staff and particularly the Stenographers and typists associated with its work.

1.9. It has not been possible for the Working Group to cover all the major issues brought to its notice, much less to deal with all the points raised by witnesses. In a later Chapter dealing with the scope of the report, the Working Group has attempted to indicate its broad approach and also to identify those major areas of company management and practice which in its judgment were of sufficient importance to need special consideration. The Working Group trust this selective approach will help to focus attention on those issues of company administration on which further thought and action would be urgently needed, if the aims and objects underlying the Act are to be substantially achieved.

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CHAPTER II

NATURE AND SIGNIFICANCE OF JOINT STOCK COMPANIES

We wish to preface our study with a brief analysis of the significance of joint stock enterprises in the economy of modern industrially advanced countries. The statistics assembled and analysed in this chapter are intended to show at a glance how during the last half a century joint stock companies even in a relatively under-developed country like ours, have grown up to their present dominant position in our economy. Their rapid growth and the increasing scale of their operations and investments constitute them as the most dominant form of economic organisation in this country, for their impact on our economic and social life far transends the immediate interests of their share-holders, creditors and their employees. It is not only in the private sector that joint stock companies have acquired this position of eminence; they have also become the standard and the most favoured forms of public enterprise.

2.2. This growth in the size and complexity of modern joint stock companies and the progressive extension of their sphere of activity have lifted them out of their original, historical, economic setting as mere legal institutions for the production and marketing of goods and services, and place them almost at the centre of the economic-life of all modern communities including ours. This has also automatically increased the economic powers exercised by them. This power is not by any means confined to the volume of goods and services which the companies produce or to the proportion of their turnover to the national aggregate of goods and services. It extends to wage rates, working conditions and other terms of labour-management relationship not only in the individual companies, but also increasingly in the rest of the organised economic sector of the country, where the norms laid down by the large joint stock companies set the pattern for others to follow. Similarly, the price policy of the individual large companies influence the course of prices in the industries to which they belong and indeed set the general price pattern in all connected industries. The consumption pattern of the community is similarly influenced both by the price and the production policies of these companies. Likewise, their investment policies through their borrowing programmes and capital issues to the public affect the resources of the investment markets while the methods adopted by them for financing and refinancing through investments largely determine the terms and conditions on which capital can be obtained by other seekers of it. The marketing systems of these companies also affect the work and fortunes of thousands of whole-salers and retailers who earn their living by selling the products of their

industries under the management of these companies. The economic and social impact on the activities of the large companies and the ramifications of their unobtrusive power enjoyed by them can be broadly assessed from this brief recital.

2.3. Dominant as is the economic impact of such large joint stock companies on the life of the modern communities whom they serve, particularly in a slowly developing country like ours, no less significant is their non-economic influence which is often over-looked in popular discussions on this subject. One of the most significant features of recent Western Literature on this subject is the analysis of the nature of this influence on society exercised by the joint stock enterprises in the modern world. We need only cite the following observations from a well-known student on this subject :—

> "Concern with the modern corporation is intensified to the extent that its activities have necessarily ramified beyond the economic sphere of production of goods and services.....Across a widening range of activity, the large corporations have become principal factors. They are the chief agencies of private research. They are the hope of fund raisers for institutions of higher learning and the principal consumers of the products of these institutions. Their advertising supports newspapers and sponsors T.V. programmes. They are a leading, if not the leading, purveyor of influence and pressure on public officials in Washington and State Capitals.....It follows that in these spheres and others they bear large American life. What has been said amounts to no more than that the great corporation is the dominant non-governmental institution of modern American life. The university, the labour union, the church, the charitable foundation, the professional association—other potential national centres—are all in comparison both peripheral and derivative."*

2.4. The statistical data which are set out in the following paragraphs do not unfortunately illustrate the type of non-economic influence to which we have referred in the foregoing paragraphs. Indeed, a major lacuna in our corporate statistics is the absence of such data. Nevertheless, within their necessarily restrictives coverage, these statistics will show the rapid advances which the joint stock companies in our country have made over the last several decades and the important role which, in our economic life, they have already begun to play.

2.5. At the beginning of this century the total number of joint stock companies with limited liability at work was 1,340 with an aggregate paid-up capital of only Rs 35 crores. At the

Vide Essay by Prof. Abram Chayes, then Prof. of Law, Harvard University in "The Corporation in Modern Society", Ed. by Prof. Edward Mason (Harvard University Press, 1961), quoted in "Towards a Philosophy of the Modern Corporation", by Shri D. L. Mazumdar (Asia—1967).

end of 1947 this number increased to 21,853 with an aggregate paid-up capital of about Rs. 480 crores.

2.6. Unfortunately during this period a large number of moribund and defunct companies misleadingly swelled and one of the first tasks of the Department of Company Affairs was to weed them out and also a considerable number of "Ghost" companies. This drive brought about a reduction in the number of companies to a total of 24,852 in 1961-62, although their aggregate paid-up capital increased to Rs. 1,974 crores, a growth rate of about 100 per cent as compared with the position in 1955-56. At the end of 1966-67 the number of companies at work was 27,247 with an aggregate paid-up capital of Rs. 3,154.4 crores.

Growth of Government Companies since 1955-56

2.7. The Companies Act of 1956 for the first time created a category of companies called Government companies. Any company in which not less than 51 per cent of the paid-up share capital is held by the Central Government or by any State Government or partly, by the Central Government and partly, by one or more State Government, is a "Government Company". The number of such Government companies at the commencement of the Companies Act in 1956 was less than 70 with an aggregate paid-up capital of about Rs. 70 crores. This number gradually increased to 232 by the end of March, 1967, and accounted for an aggregate paid-up capital of about Rs. 1,392 crores.

2.8. Table I shows the growth in Government and non-Government Companies for the years 1956-57 to 1966-67 and Table II summarises the net increase in the paid-up capital of Government and non-Government Companies during the period.

TABLE I

Number and paid-up Capital of Government and non-Government Companies : 1956-57 *to* 1966-67

(Capital in crores of Rs.)

Year ending the 31st March	All Companies		Government Companies		Non-Government Companies	
	No.	Paid-up capital	No.	Paid-up capital	No.	Paid-up capital
1957 ..	29,857	1,077·6	74	72·6	29,283	1,005·0
1958 ..	28,280	1,306·3	91	256·8	28,189	1,049·5
1959 ..	27,403	1,515·6	104	428·9	27,299	1,086·7
1960 ..	26,897	1,618·7	125	477·2	26,772	1,141·5
1961 ..	26,149	1,818·5	142	547·0	26,007	1,271·5
1962 ..	24,975	2,019·1	154	629·7	24,821	1,389·4
1963 ..	25,622	2,256·3	160	786·0	25,462	1,470·3
1964 ..	25,932	2,603·1	176	960·8	25,756	1,642·3
1965 ..	26,584	2,779·4	183	1,114·9	26,401	1,664·5
1966 ..	27,010	2,948·6	214	1,247·7	26,796	1,700·9
1967 ..	27,247	3,154·4	232	1,391·5	27,015	1,762·9

TABLE II

Net increase in the paid-up Capital of Government and Non-Government Companies at work : 1957-58 to 1966-67

(Capital in crores of Rs.)

Year	Total Companies	Government Companies	Non-Government Companies
1957-58 ..	229·3	184·8	44·5
1958-59 ..	209·3	172·1	37·2
1959-60	103·1	48·3	54·8
1960-61 ..	199·8	69·8	120·0
1961-62 ..	200·6	82·7	117·9
1962-63	237·2	156·3	80·9
1963-64	346·8	174·8	172·0
1964-65 ..	176·1	154·1	22·0
1965-66 ..	135·8	99·4	36·4
1966-67 ..	239·2	177·2	62·0

2.9. It will be seen from these two Tables that although Government companies formed only a small part of the total number of companies at work (232 out of 27,247), their aggregate paid-up capital accounted for over two-fifth of the entire paid-up capital. During the period from 1957-58 to 1966-67, the increase in their paid-up capital however was higher than the increase in the paid-up capital reported by non-Government companies. This remarkable increase in the Government companies was due to the establishment of such giant-sized companies in the public sector as the Hindustan Steel Ltd., the Neyveli Lignite Corporation Ltd. the Fertilizers Corporation of India Ltd.; the National Coal Development Corporation Limited; the Indian Refineries Ltd.; and the Heavy Electricals (India), Ltd.

Company Registrations from 1956-57 to 1966-67

2.10. The trends in company registrations during this period also give some indication of the rate of growth of the corporate sector. At the time of the coming into force of the Companies Act in 1956, fears were expressed even in some knowledgeable circles that due to the restrictive provisions of the Act, Company registrations in future might receive a set-

back. The statistical data in the two Tables which follow, belie this apprehension :—

TABLE III

New Government Company Registrations 1956-57 *to* 1966-67

(Authorised Capital in lakhs of Rs.)

Year	No.	Public Authorised Capital	No.	Private Authorised Capital	No.	Total Authorised Capital
1956-57 ..	..	..	13	120	13	120
1957-58 ..	1	10	17	850	18	860
1958-59 ..	..	..	16	98,31	16	98,31
1959-60 ..	1	1,00	22	29,10	23	30,10
1960-61 ..	..	..	17	31,39	17	31,39
1961-62 ..	1	50,00	17	72,71	18	1,22,71
1962-63 ..	3	4,50	5	16,00	8	20,50
1963-64 ..	7	35,00	12	1,34,65	19	1,69,65
1964-65 ..	4	9,00	11	66,69	15	75,69
1965-66 ..	8	20,55	20	83,10	28	1,13,65
1966-67 ..	3	13,65	15	46,90	18	60,55
Total ..	28	1,43,80	1,65	5,88,55	1,93	7,32,35

TABLE IV

New Non-Government Company Registrations 1956-57 *to* 1966-67

(Authorised Capital in lakhs of Rupees)

Year	Public		Private		Total	
	No.	Authorised Capital	No.	Authorised Capital	No.	Authorised Capital
1956-57 ..	84	54,13	751	36,52	935	90,65
1957-58 ..	64	52,64	879	41,47	943	94,11
1958-59 ..	58	8,67	1,021	1,27,38	1,079	1,86,05
1959-60 ..	86	66,14	1,343	64,30	1,429	1,30,44
1960-61 ..	153	1,57,50	1,513	98,16	1,666	2,55,66
1961-62 ..	198	129 20	1,398	72.96	1,596	2.02.19
1962-63 ..	224	1,70,86	1,265	66,19	1,489	2,37,05
1963-64	148	1,13,25	1,060	57,59	1,208	1,80,84
1964-65 ..	176	1,39,54	1,174	64,54	1,350	2,04,08
1965-66 ..	124	1,00,46	1,189	61,08	1,313	1,61,54
1966-67 ..	79	48,29	942	52,38	1,021	1,00,67

2.11. The noticeable fall in the new registrations after 1962-63 is an index to the continuing sluggish condition of the new issue market, since the Chinese attack on our northern borders from which it has yet to recover adequately.

Public Limited and Private Limited non-Government Companies

2.12. The Companies Act at present makes an important distinction between public limited and private limited companies, as several Sections of the Act do not apply to private limited Companies. We have considered the question of proper re-classification of companies in Chapter V of this Report. It may, however, be useful in this context to reproduce briefly the data relating to public limited and private limited companies at work from 31st March, 1956, i.e., just before the coming into force of Companies Act of 1956 to date, in so far as non-Government Companies are concerned.

2.13. Table V shows break-up of non-Government companies at work separately for public limited and private limited companies and also their aggregate paid-up capital.

TABLE V

Non-Government Companies at Work

(Capital in crores of rupees)

Year ended	Public		Private		Total	
	No.	Paid-up Capital	No.	Paid-up Capital	No.	Paid-up Capital
31-3-1956 (a) ..	9,575	690·4	20,299	333·8	29,874	1,024·2
31-3-1957 ..	8,771	695·7	20,512	309·3	29,283	1,005·0
31-3-1958 ..	8,255	755·5	19,934	293·9	28,189	1,049·5
31-3-1959 ..	7,608	782·2	19,691	304·5	27,299	1,086·7
31-3-1960 ..	7,151	814·1	19,621	327·4	26,772	1,141·5
31-3-1961 ..	6,663	915·2	19,344	356·3	26,007	1,271·5
31-3-1962 ..	6,399	1,093·3	18,422	296·1	24,821	1,389·4
31-3-1963 ..	6,404	1,170·6	19,058	299·7	25,462	1,470·3
31-3-1964 ..	6,474	1,281·0	19,282	361·3	25,756	1,642·3
31-3-1965 ..	6,492	1,328·6	19,909	335·9	26,401	1,664·5
31-3-1966 ..	6,410	1,346·0	20,386	354·9	26,796	1,700·9
31-3-1967 ..	6,309	1,401·8	20,706	361·1	20,015	1,762·9

(a) Includes companies which on 1st April, 1956 became Government companies

2.14. It would be seen from this Table that although at present there are over 27,000 non-Government companies at work, 6,309 public limited companies with an aggregate paid-up capital of Rs. 1,402 crores account for nearly four-fifths of the aggregate paid-up capital of all companies at work.

2.15. The remarkable growth in the public limited corporate sector during the last few years has been substantially led by the financial institutions, such as the Life Insurance Corporation, the Industrial Credit & Investment Corporation of India, the Industrial Finance Corporation, the Industrial Development Bank, the Unit Trust of India, etc., which have increased their share of under-writing the issues of public limited companies. Tables VI and VII show the amount of capital under-written by these institutions in the form of share issues and debentures capital, respectively.

TABLE VI

Amount under-written by leading under-writers during the years 1962-63 *to* 1967-68 (*Share Issues*)

(Amount in lakhs of rupees)

	1962-63	1963-64	1964-65	1965-66	1966-67	1967-68
1. L.I.C. ..	119.4	167.5	360.0	390.0	319.5	432.3
2. I.C.I.C.I. ..	32.5	157.5	281.0	218.0	211.1	237.0
3. I.F.C. ..	50.4	238.0	300.0	285.0	164.5	75.5
4. I.D.B.I. ..	..	..	106.0	577.0	408.7	61.5
5. U.T.I. ..	..	..	29.8	45.0	85.7	185.0
6. State Govts. ..	..	48.4	57.0	26.0	..	10.0
7. State Finance Corporations ..	22.5	220.5	396.0	412.0	191.8	140.3
8. Others ..	581.0	952.9	864.5	689.0	439.8	925.9
Total ..	805.8	1784.8	2394.3	2642.0	1821.1	2067.5

TABLE VII

Amount under-written by leading under-writers during the six years 1962-63 *to* 1967-68 (*Debenture Issues*)

(Amounts in lakhs of rupees)

	1962-63	1963-64	1964-65	1965-66	1966-67	1967-68
1. L.I.C. ..	850.0	313.0	625.0	175.0	343.0	415.0
2. I.C.I.C.I. ..	250.0	130.0	235.0	140.0	234.0	237.0
3. I.F.C. ..	350.0	..	135.0	95.0	75.0	65.0
4. I.D.B.I. ..	..	..	..	40.0	50.0	..
5. U.T.I. ..	..	..	525.0	105.0	175.0	339.7
6. Others ..	705.0	247.0	388.0	255.0	384.5	457.0
Total ..	2155.0	390.0	1908.0	810.0	1261.5	1213.0

2.16. The above figures will bring out the important part which these financial institutions play in the new issue market. Since a large part of the capital under-written by these institutions has been subscribed by them these financial institutions have in the process also become important share-holders in public limited companies and constitute the back-bone of the 'Committed' shareholders who play an increasingly important role in the management of public companies and the maintenance of standards of management in the industrially advanced countries of the West. We have discussed elsewhere in this Report the role which we expect these financial intermediaries to play in improving the efficiency of the corporate sector in future.

2.17. We in the Working Group are mainly concerned with incorporated companies, but the responsibilities of the corporate sector apply equally to unincorporated business and sooner or later such business may choose to get itself incorporated. We have, therefore, looked into such data relating to the growth of incorporated and unincorporated business in this country as are available from the Income-tax statistics. Table VIII shows the growth of unregistered firms, registered firms and companies.

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TABLE-VIII

Growth of Unregistered Firms. Registered Firms and Companies

	Number of Assessees							
	1956-57	1957-58	1958-59	1959-60	1960-61	1961-62	1962-63	1963-64
I. Number—								
(a) Unregistered Firms and Associations of Persons	23,458	28,279	33,221	29,488	27,708	29,556	25,473	25,877
(b) Registered Firms ..	6,551	9,330	11,372	14,179	15,396	17,712	30,437	33,741
(c) Companies ..	10,780	10,939	10,778	9,791	9,959	11,464	12,024	10,315
Total ..	40,789	48,598	55,371	53,458	53,063	58,732	68,934	69,933
II. Rate of Increase over 1956-57—								
(a) Rate of annual increase in Unregd. Firms ..	20.6	41.6	25.7	18.1	16.0	26.0	12.9	10.3
(b) Rate of annual increase in Regd. Firms	..	42.4	73.6	116.4	135.0	170.4	364.6	415.1
(c) Rate of annual increase in Cos.	..	1.9(—)	0.002(—)	9.1(—)	7.6	6.3	11.5	(—)4.3
(d) Rate of total annual increase—	..	19.1	35.7	31.1	30.0	44.0	69.0	71.5
III. Importance of each category of business—								
(a) Unregistered Firms and Assocns. of persons as per cent of total ..	57.5%	58.2%	60.0%	55.2%	52.2%	50.3%	38.4%	37.0%
(b) Regd. Firms as per cent of total ..	16.1%	19.2%	20.5%	26.5%	26.5%	30.2%	44.2%	48.2%
(c) Companies as per cent of total ..	26.4%	22.6%	19.5%	18.3%	18.8%	19.5%	18.4%	14.9%

2.18. It will be seen from this Table that the two categories of assessees known as "Unregistered Firms and Associations of persons" and "Companies" have not recorded any substantial increase in 1963-64 as compared with 1956-57; whereas the class known as "Registered Firms" have reached the highest figure of 33.741 as against 6,551 in 1956-57. In fact, "Unregistered Firms and Associations of Persons" registered a continuous fall in number during the period 1959-60 to 1963-64 but was still higher during the period 1963-64 as compared with the base year consequent on a large increase during 1957-58 and 1958-59. In so far as the "Companies" are concerned it will be seen that they came down in number from 1958-59 to 1960-61, went up during 1961-62 and 1962-63 but slided back once again in 1963-64, as compared with the base year of 1956-57.

TABLE IX

Growth in income of different forms of Business

(Rupees in crores)

	Income Assessed							
	1956-57	1957-58	1958-59	1959-60	1960-61	1961-62	1962-63	1963-64
Income—								
(a) Unregistered Firms and Associations of Persons	32.7	34.5	37.9	34.9	31.9	39.3	35.3	34.9
(b) Registered Firms	51.9	74.2	90.2	112.5	127.5	148.7	197.4	205.0
(c) Companies	235.9	219.7	265.9	213.0	247.9	405.0	361.2	271.5
Total I	320.5	328.4	394.0	360.4	407.0	593.0	593.9	551.4
II. Rate of Increase over 1956-57—								
(a) Rate of Annual Increase in Unregd. Firms		5.5	15.9	6.7	(—)2.4	20.2	7.9	6.7
(b) Rate of annual increase in Regd. Firms		43.0	73.8	116.8	145.7	186.5	230.3	295.0
(c) Rate of annual increase of companies		(—)6.9	12.7	(—)9.7	5.1	71.7	53.1	15.1
(d) Rate of total Annual increase		2.5	22.9	12.3	27.1	85.0	85.3	59.6
III. Importance of each Category of Business—								
(a) Unregistered Firms and Associations of Persons as per cent of total	10.2	10.5	9.5	9.7	7.8	6.6	5.9	6.8
(b) Registered Firms as per cent of total	16.2	22.6	22.9	31.2	31.3	25.1	33.3	40.1
(c) Companies as per cent of total	73.6	66.9	67.5	59.1	60.9	68.3	60.8	53.1

2.19. Table IX analysis the growth in income of the various firms of business during 1956-57 to 1963-64. "Unregistered Firms and Associations of Persons" recorded an increase of 6.7 per cent in 1963-64 as compared with 1956-57, while "Registered Firms" increased by 295 per cent and "companies" by 15.1 per cent. Table IX also shows the importance of each category of business organisation in relation to the total income assessed to tax during the period. The importance of "Registered Firms" increased from 16.2 per cent in 1956-57 to 40.1 per cent in 1963-64. On the other hand, the importance of the other two forms of business organisation, viz., "Unregistered Firms and Associations of Persons" and "Companies" declined from 10.2 per cent to 6.8 per cent from 73.6 per cent to 53.1 per cent, respectively. Judged by the amount of income assessed to tax, "companies" occupied a very high place in 1956-57, and although their relative rating from this point of view declined in 1963-64, they still continue to be the leading form of business organisation.

2.20 Table X shows the growth in the realisation of tax from different forms of business organisation between 1956-57 and 1963-64. It would be seen from Table X that during the entire period "Unregistered Firms and Associatinos of Persons" declined by about 3.8 per cent; whereas both "Registered Forms" and "Companies" increased, respectively by 481.3 per cent and 25.5 per cent. It will also be seen from Table X that the importance of "Unregistered Firms and Associations of Persons" in the total tax collections declined during the same period from 6.7 per cent in 1956-57 to 4.9 per cent in 1963-64. A similar decline is also seen in the case of "Companies" whose importance in the total tax collection declined from 91.9 per cent in 1956-57 to 89.0 per cent in 1963-64. On the other hand, "Registered Firms" increased their share from 1.4 per cent in 1956-57 to 6.1 per cent in 1963-64.

TABLE-X

Growth in Tax realisations from different forms of Business Organisation

TAX

	1956-57	1957-58	1958-59	1959-60	1960-61	1961-62	1962-63	1963-64
I. Tax—								
(a) Unregistered firms and Associations of Persons	7.9	6.8	7.4	7.6	6.2	8.7	7.3	7.6
(b) Regd. Firms ..	1.6	2.3	2.7	3.5	4.1	4.9	7.8	9.3
(c) Companies ..	108.5	110.5	137.4	109.5	122.0	195.9	175.1	136.2
Total ..	118.0	119.6	147.5	120.6	132.3	209.5	190.2	153.1
II. Rate of Increments over 1956-57—								
(a) Rate of annual increase in unregistered firms ..		(—)13.9	(—)6.3	(—)3.8	(—)21.5	10.1	(—)7.6	(—)3.8
(b) Rate of annual increase in Regd. Firms ..		43.8	68.8	118.8	156.3	203.3	387.5	481.3
(c) Rate of annual increase in companies ..		1.8	26.6	0.9	12.4	80.6	61.4	25.5
(d) Rate of Total Annual Increase ..		1.4	25.0	2.2	12.1	77.5	61.2	29.7
III. Importance of each category business—								
(a) Unregistered Firms and Associations of Persons as per cent of total ..	6.7	5.7	5.0	6.3	4.7	4.2	3.8	4.9
(b) Registered Firms as per cent of total ..	1.4	1.9	1.8	2.9	3.1	2.3	4.1	6.1
(c) Companies as per cent of Total ..	91.9	92.4	93.2	90.8	92.2	93.5	92.1	89.0

2.21. Although by number, unincorporated business is much higher than Companies, from the point of view of tax collected, Companies stand head and shoulders above the other forms of business organisation.

2.22. Table XI shows the importance of the corporate sector in relation to the national economy.

Table—XI

Some Indicators of the size of Corporate Sector

	1960	1963	1964	1965	1966	1967
1. Total number of Joint Stock Companies at work ..	26,897	25,622	25,932	26,584	27,010	27,247
2. Total paid-up capital investment (Rs. in crores)	1,619	2,256	2,603	2,779.4	2,948.4	3,154.4
		1957	1961	1963	1965	1966
3. Total sales or main income of companies (Rs. in crores)		3,700	5,210	6,132	9,806	10,892
4. Total Assets (net of depreciation) of companies (Rs. in crores) ..		3,650	4,850	5,856	10,244	11,425
				1957	1961	1963
5. Share of companies in the net domestic output—						
Total net domestic output (Rs. in crores) ..				11,400	14,960	15,480
Output of companies (Rs. in crores) ..				1,310	1,890	2,390
Share of companies ..				12%	13%	15%
				1957	1961	1962
6. Share of companies in tax revenue of Central Government—						
Total tax demands (Rs. in crores) ..				222	243	322
Tax Demands from companies (Rs. in crores) ..				111	122	159
Share of companies ..				50%	50%	50%

	1960-61	1963-64	1964-65	1965-66	1966-67	1967-68
7. Share of Corporate Tax raised from companies in the total revenue of Central Government—						
Corporate Taxes (Rs. in crores)	135	227	295	305	329	320
Total revenue (Rs. in crores)	1,086	1,852	2,095	2,490	2,731	2,813
Share of Corporate Taxes ..	12%	12%	14%	12%	12%	11%

	1956	1958	1961
8. Share of companies in the factory output (30 industries)			
Total output of all factories (Rs. in crores) ..	1,614	1,711	3,693
Output of company owned factories (Rs. in crores)	1,318	1,395	..
Share of company owned factories ..	81.7%	18.5%	..
9. Share of companies in the production of factories ..	1956	1958	1961
Total Productive capital (Rs. in crores) ..	1,004	1,215	2,374
Productivity capital of co. owned factories (Rs. in crores) ..	889	1072	..
Share of capital owned factories ..	88.5%	88.2%	..

It will be seen from Table XI that in 1967 out of the estimated revenue budget of Rs. 2,813 crores, as much as Rs. 420 crores, i.e. nearly 11 per cent of the revenue budget was expected to be realised from the corporate sector. Corporate sector also accounts for nearly 9/10ths of the productive capital of all factories in the country.

2.23. Table XII shows the share of the corporate sector in the total net domestic product at factor cost. It will be seen from this that the corporate sector contributes over 1/10ths of the national income of the country.

Table—VII

Share of the Corporate Sector in the Total Net Domestic Product at Factor Cost.

	1948-49	1950-51	1956-57	1957-58	1960-61	1962-63
Share of the Corporate Sector in the total net domestic product at factor cost ..	7%	8%	11%	12%	13%	15%
Share of the Corporate Sector (excluding Government Companies) in the total net domestic product at factor cost for the non-Government companies ..	8%	10%	12%	11%	12%	11%

2.24. In the previous paragraphs we have set out some significant data relating to the importance and growth of the corporate sector in order to bring out its role in the economy of the country. With the progress of industrialisation this role will rapidly grow.

The efficient management of companies is, therefore, a matter of concern not only to the shareholders and the other interests connected with their working but also to the national economy and the public interest.".

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CHAPTER III

CHANGING CONCEPT OF COMPANY LAW IN THE CONTEXT OF MODERN THINKING ON THE SUBJECT

The problems relating to the administration of Company Law and other connected measures and agencies which closely affect the working of joint stock companies cannot be adequately appreciated, unless they are considered in the perspective of contemporary thinking on the nature and role of joint stock companies in the economy of most modern industrialised countries. That is why we referred in the previous chapter to present day thinking on the responsibilities of the modern corporation. As was indicated there, the relevant literature on the subject of the growth and development of corporate enterprise in the Western World, and similar literature such as is available albeit to a limited extent in this country, has already analysed the factors which brought about a major change in the character and significance of joint stock companies well before World War II. It is, however, only during the last two or three decades that scholarly recognition of the economic and social consequences of this change has slowly brought about a radical transformation in the thinking on Company Law. In the result, in recent years, recommendations have been made in many Western Countries for far reaching innovations in the structure of this law which, in the nineteenth and early twentieth century concepts of company law, would have been considered completely alien to its traditional aims and objects. In the present context it is unnecessary to dilate on the circumstances leading to this development, much less to try to document the steady growth of ideas for the reform of the law. It will suffice to produce the following extracts from a latest broadsheet, entitled 'A Companies Act, 1970', prepared by Political and Economic Planning, a well-known research organisation in the U.K. concerned with the study and analysis of economic and social problems, which acts as bridge between research on the one hand and policy making on the other. We do not apologise for the length of these citations. For, not only do they neatly delineate the broad parameters of the new thinking but also bring out succinctly its policy implications which are still not sufficiently known to or appreciated by most practitioners or professional students of this subject in this country.

"In the last few years the foundations of corporate enterprise have been questioned across the world to an extent not seen for decades. In the United States large companies have

been forced to think harder than in the past about their social reponsibilities both at home and overseas. More and more of them have found it advisable to establish a "public affairs function" as a distinct part of their organisation. In American business schools there has been an increased accent on courses on the firm's overall priorities and strategy under titles such as, 'Planning in the Business Environment'. Germany and France have recently not merely amended their Company law but comprehensively revised it, with far-reaching innovations in areas such as the authority and accountability of managing directors, the relations between holding companies and their subsidiaries. Comprehensive revisions are also on the way in Belgium, Holland and Italy. Belgium and Holland are moving towards the German two-board system. In Holland, the most recent company law commission, the Verdam Commission on Enterprise Law Reform, has proposed that the Supervisory Boards of Public Companies and their subsidiaries should include employee representatives, and that employees and other parties as well as shareholders should be able to call for the equivalent of a Board of Trade enquiry. In Italy a new form of public supervision has been proposed for quoted companies.....".

"These developments, whether in the East or the West, have of course given rise to much controversy as well as being the outcome of it. Many of them have been coloured with ideology, history, or a mixture of the two.....". But the overall impression is that, when the debate is over and the interest groups have had their say, what is happening is not a distortion of the development of the corporation by this or that interest or ideology but the progressive adaptation of businesses and of those who manage, regulate and influence them to the actual logic of a mixed economy in which many interests have to be reconciled and both competition and planning have a part to play. East European businesses have moved towards a more Western pattern, not because their leaders have turned capitalists, but because a market economy has proved useful in a socialist as well as capitalist framework and its logic has to be respected. American corporations are recognising a distinct public affair function not because they have turned soialist but because a large corporation in a modern economy inevitably develops a network of relationships with Governments (at home or abroad), local authorities, and a wide range of other social institutions. These relationships like any other branch of management must be handled in an expert and organised way. They have also to be co-ordinated, for a company, whether it intends to or not, develops an overall image which influences customers, recruits, and the company's standing with public authorities....."

"The pressure for change in the law and practice of corporations has come from conservatively minded lawyers and economists or from bodies such as shareholders' associations as well

as from radical politicians, trade unionists and in some countries the clergy. One cannot say that it is the Right and the employers who put forward "conservative" reforms such as the technical tidying up of traditional company law while the left and the trade unions press for more far reaching measures of employee participation and public control. In France the most radical thinking about employee participation and public control, and indeed about the reform of classical company law itself, has come not from the Left and the unions but from the technical and managerial elite whether in business or in the civil service, and from nationalist politicians supporting General de Gaulle. German employers and associations part company with German unions on the question whether employees should have equal representation with shareholders on Supervisory Boards, but otherwise hold views about employees on boards, about statutory works councils, including councils' rights to information and to appeal to outside arbitration on issues such as major redundancy, and about employee shareholding, which would seem decidedly left-wing elsewhere in the West."

"Britain till recently was rather slow to take part in this reconsideration or corporate enterprise..... The Cohen Committee on Company Law, which was set up during the war, was instructed :

> "To review the requirements prescribed in regard to the formation and affairs of companies and the safeguards afforded for investors and for the public interest. (*)

"The reference to the public interest is particularly striking..... ....."

> "Even at that time, however, reforms in the structure of private corporations were not in the centre of the political picture, nor were these corporations' traditional principles challenged.....".

"This has now changed. One factor has been better knowledge of new thinking in other countries, particularly of developments in the European Community in which Britain may become directly involved. Another, more immediately important, has been the sheer pressure of facts in two areas, industrial relations and national, regional, and local planning.... ....."

"The Government for its part has announced that it will bring in before the end of the present Parliament, that is at the latest by 1970 or early 1971, a Companies Bill which will :

> "Re-examine the whole theory and purpose of the limited joint stock company, the comparative rights and

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(*) Report of the Committee on Company Law Amendment, (The Cohen Committee), Cmd. 6659, 1945, p. 2.

obligations of shareholders, directors, creditors, employees, and the community as a whole."(*)

"Views will of course differ widely on many of the issues examined here, and a number are outside what was still recently the main stream of British discussion on Company reform. But whereas a few years ago, at the time of the Jenkins Committee, the fact that a proposal for company reform was novel or fundamental was enough to rule it out of consideration even on the Left, today this is ceasing to be so. Proposals for fundamental change, whether in the interests of the efficiency of firms and the economy or of the satisfaction of employees and the community, are receiving wide and serious consideration. Which of them will have priority and what weight of support is behind any of them can still only be guessed. But in a general way the idea that there might be basic changes in company law has moved out of the realm of theory into that of serious political discussions. Important political and social forces have become interested in it and can influence Government action. It is, therefore, necessary that any proposals which might have a chance of practical consideration should be brought into the open and debated in good time ....." (**)

3.2. This debate was initiated in this country, albeit in a somewhat different milieu and context over more than a decade ago. The policy decisions which emerged out of this debate have since been embodied in several major provisions of the Companies Act, 1956, which break entirely new ground in several areas, notably in those relating to managerial appointments and compensation and management practices. Many of these provisions appeared at that time to be novel and strange to those who had been brought up on the traditional view of company law and its contents and still clung to them. That mood, however, still continues to linger in some quarters. But all those who are at present operationally involved in company affairs now need to view our Companies Act of 1956 in the light of these recent developments in informed thinking on the role and scope of Company Law in the industrially advanced countries of the world.

3.3. Historically, till 1956 our successive Companies Acts very closely followed the structure and contents of the corresponding Companies Acts in the United Kingdom. So the proposals for the reform of this law, which were for the first time initiated in a big way in the inter-war years resulting in the amendment of the Act in 1937, were concerned primarily with the abuses in company management deriving largely from

(*) President of the Board of Trade, U.K., House of Commons Debates, February, 14, 1967, Col. 359.

(**) *Vide* A Companies Act, 1970—Political and Economic Planning Board Sheet, Vol. XXXIII, No. 500 (October, 1961, pp. 69—79).

the Managing Agency system as it was then operated. The later proposals for reform of the law initiated and debated between 1946 and 1953 were also largely coloured by the same concern to prevent large scale malpractices which had disfigured company management in the circumstances generated by World War II and its aftermath. Thus the first version of the Companies Bill, 1953, introduced in Parliament was dominated by this concern, and was very much in the main stream of the traditional thinking of Company Law reformers in the Western world of an earlier generation. During the progress of this Bill, however, several far-reaching innovations were introduced into it, in the wake of the newly-formulated goals of the then evolving social and economic policy of the country which culminated in the adoption by Parliament in early 1955 of the resolution on the Socialist Pattern of Society as the ultimate goal of the country's economic and social policies. This was the second broad strand of thought that left a distinctive stamp on the Companies, Act, 1956 as it finally emerged out of the legislature, It is these innovations, mostly relating to company management and company practice, that constituted a major departure from the traditional structure of company law.

3.4. The impulse behind these innovations owed its origin to historical, economic and sociological factors in this country, which were in several ways different from the comparable circumstances which led to the evolution of the new thinking in the Western World, but in so far as their roots go down to our newly-evolved national, economic and social policies, they are in a sense close to the mainstream of those basic forces which had shaped and conditioned contemporary thinking on company law in many other parts of the modern world. This only illustrates the true nature of the growth of legal concepts and norms. Irrespective of the different parts played by political, economic or social ideology in generating legal innovations, law in all countries is inevitably influenced by changes in the domestic economic and social forces. The time-lag between the emergence of these forces and their impact on law. however, varies from country to country.

3.5. This change in the character of our Company Law renders the task of its implementation and enforcement specially difficult. For Administration cannot confine itself merely to interpretation of the words of the statute, but is called upon to exercise purposive judgment over a wide field, in which a balanced view of the values implicit in the new provisions of the Act of 1956 has to be taken in the light of the facts and circumstances of individual cases. This requires that not only should there be sufficient flexibility in the administration of the law based on a realistic but discriminative understanding of the needs of individual enterprises, but the Administrators must also possess the capacity to adjust them suitably within the

broad frame of the general policies embodied in the relative provisions of the law. This calls for not only adequate professional competence but also a high degree of discernment and mental resilience on the part of administrators.

3.6. It is, however, necessary in this context to stress the fact that there are some essential pre-conditions to the purposeful and effective administration of the Companies Act and related matters. These are—(a) first, that the policies embodies in the provisions of the Act should be spelt out with sufficient concreteness so that there may be no difficulty in translating them into operational terms; (b) secondly, there should be a reasonable measure of commitment to these policies, alike on the part of Ministers and other policy-makers connected with their administration and of the senior civil servants entrusted with their implementation responsibility; (c) thirdly, the relevant statutory provisions should be reasonably free from ambiguity; and (d) fourthly, the executive rules, regulations and instructions framed under the statute with due regard to good company practice should be clearly worded and internally consistent.

One of the major handicaps to the administration of our Companies Act since its early days has stemmed from the fact, that these conditions have never been adequately fulfilled whether at the political and/or the administrative level. The broad political consensus arrived at in the mid-fifties on the ultimate aims and objects of the country's economic and social policies did not, however, reach down to the details of these policies or their pragmatic implications. In the result, Administration lacked a clear focus of light to guide it in the twilight region of the new values with which many provisions of the Companies Act were impregnated. We do not wish to pursue further these basic quasi-political hurdles from which the administration of the Companies Act has suffered much in the past. But we consider it necessary to underline them at this stage, so that in any comprehensive assessment of the perfomance of the Administration, this important fact may not be overlooked.

3.7. Within the limits of the basic considerations set out above, the efficiency and effectiveness of Administration would depend a great deal on their education and training of the administrators. Equally important is the need for working out a network of communication as between the administrators and the administered, through which the meaning and relevance of the prescribed rules and regulations and executive instructions can be disseminated among the senior company executives and their professional advisers on the one hand and junior ranks of the Administration on the other. It is only on this basis that informed understanding and accord can be established between the administrators and the management of business enterprises, and the purposes underlying the Act can be better achieved.

CHAPTER IV

SCOPE OF THE REPORT

What we have stated in the previous Chapter about the factors which have shaped and developed our Company Law and the difficulties in its administration stemming largely from the complicated nature of the objectives which the Law is intended to achieve, does not imply any judgment on the policies finally embodied in the existing provisions of the Companies Act. Although the statute in its present form embodies the broad consensus reached during the parliamentary debates on the subject, we are aware that critical views on some of these policy decisions had been expressed in the past and similar comments still continue to be made from time to time. Our terms of reference, as we view them, are primarily concerned with the administrative problems connected with the enforcement of the Act, arising from the present organisation of the machinery of administration for this purpose, and the procedures laid down in the Act and in the rules and regulations framed by the Administration to give effect to the policies embodied in the operative provisions of the Act. These necessarily affect the pace and mechanics of Administration and also the responses and reactions of the members of the business community who are required to comply with them. Our task is, therefore, also to consider the nature of the impact of the procedural requirements of the law on business as well as administration—to find out to what extent the prescriptions of the statute and the rules and regulations framed by the Administration under the powers vested in it impose avoidable burden both on those who are connected with the management and working of companies and also on administrative personnel concerned with their enforcement. Further, we have been asked to assess the extent to which the present Act and the manner in which it has been administered helps to achieve the social and economic policies underlying its substantive provisions. Lastly, our terms of reference enjoin us to consider what changes, if any, are necessary in the present administrative set up for the better co-ordination of work among the multiple authorities now dealing with matters closely bearing on the corporate sector and more expeditious and purposeful administration, and how the existing administrative capabilities in this area can be strengthened and developed.

4.2. We consider it necessary to bring out these major elements in our terms of reference in order to indicate in advance the scope and limitations of our Report. We have not construed our task as that of a committee or commission primarily concerned with the amendment of the Act or of the rules

and regulations framed under it. In course of the evidence recorded by us at different centres, many witnesses, particularly those belonging to the legal and accountancy professions, have drawn our attention to several defects and lacunae in the Act, to apparent inconsistencies in the interpretation of some of its provisions and not so apparent incongruent policies embodied in the provisions of other related statutes. We have taken note of this evidence and referred to some of these points in a subsequent chapter of our report. But we do not consider that these suggestions for the *technical* improvements of the law fall within the mainstream of our enquiry. We would, however, note in this context that the Companies Act, 1956 has been amended almost annually since 1963 and some further amendments, we understand, are in the offing in course of this year. Whatever may be the reasons for these frequent amendments, it would not be unfair to infer that they were conceived and designed primarily to deal *ad hoc* issues, which arose from time to time and which could not obviously have been based on any total view of company law and its bearing on the working of joint stock companies.

We, therefore, suggest that a comprehensive look at the detailed provisions of the Companies Act and also of the other related statutes, some of which are at present administered by other ministries and departments, should be undertaken at an appropriate time as soon as the Legislature has dealt with the Monopolies and Restrictive Trade Practices Bill which, we understand, is now before a Select Committee of Parliament.

If an integrated Ministry to deal with company affairs is established at an early date, in purusuance of one of the recommendations which we propose to make later in this report, this overalll review of the technical provisions of the law would be rendered much easier. Our suggestion for a comprehensive study of the companies and other related Acts is not, however, tied up with this recommendation. The issue is of sufficient importance in itself to justify early action alike in the interest of administration and business community. The object of this overall review which we suggest would be to undertake a detailed study of the specific provisions of the Act in relation to the other related Acts with a view to—

(a) co-ordinating and integrating the policy decisions embodied in these provisions and now administered by different departments in an un-co-ordinated and fragmentary manner; and

(b) assessing the total burden imposed on the Administration in order to find out how much of it could be reduced through changes in the technical requirements

of the law and better co-ordination and integration of the administration of other statutes now administered by other ministries and departments

4.3. We have not had adequate time also to go through the numerous returns and statements which the Act and the rules and regulations framed under it require to be submitted to the Administration.

We would, therefore, also recommend the setting up of a competent expert committee to go into this subject.

Several witnesses referred to the burden cast on the business community and the professions connected with the working of companies by this requirement and suggested that many of them might be simplified, amalgamated, abridged and even deleted. We had a case study prepared on this subject by the departmental officers. This case study goes into the nature and purposes of these returns and statements and tries to explain why they are necessary. We are aware that many of these returns were prescribed on the basis of similar returns submitted under the Companies Act in U.K. We also recognise the fact that a large number of them are intended for the benefit of the shareholders and the creditors of the companies and that, in any case, the office of the Registrar of Joint Stock Companies is an office of public record to which all those who are directly or indirectly connected with the working of the companies turn for information relating to them. Nevertheless, we consider that time has come when there is need to have a detailed scrutiny of these returns bearing in mind the purposes for which they were originally conceived, but at the same time taking into account the actual use that is made of these returns in the offices of the Registrars. We shall revert to this question in a latter chapter of our report. For the present we refer to it only to indicate the scope of our report.

4.4. Within the broad frame of policy as embodied in the principal substantive provisions of the Act, we have considered it desirable to concentrate only on those major areas of law and administration in respect of which we felt that suitable changes in existing policy or practice might reduce the work-load on the Administration without material damage to policy aims and objects; or where in our judgment alternative methods of work might help to improve the efficiency of administration; or where certain processes and procedures could be changed or modified without any damage to the purposes of the law. In this view we have in the subsequent chapters of our report concentrated on the following major topics:—

(i) the classification of companies as private and public;
(ii) the structure of company management;

(iii) the existing pattern of direct control over company management;

(iv) problems arising from the exercise of discretionary authority by the Administration over a large area of company management and practice;

(v) the present organisation for the administration of Company Law, including administrative problems connected with the inspection, investigation and prosecution of company cases;

(vi) the problem of the integration of company administration with the administration of financial and other institutions connected with the working of companies;

(vii) the present organisation for dealing with the winding up of companies;

(viii) the problems connected with the present organisation for judicial review of company laws and other company matters where such review is needed under the provisions of the Act, and other matters arising out of the administration of the Act.

(ix) A few other important matters which in our opinion have a close bearing on the working of companies.

4.5. As we have endeavoured to emphasise in the foregoing paragraphs, these topics do not cover all the major areas of company law and company administration but for reasons already explained we have considered it desirable, within the limits of time at our disposal, to concentrate on the above areas.

CHAPTER V

Classification of Companies

We received a considerable volume of evidence on the need for a revised classification of companies under the Companies Act. The importance of this subject arises from its relevance to the better administration of the Companies Act as well as to the more effective achievement of some of the basic purposes underlying the Act. It was argued by witnesses before us that it was unnecessary to subject relatively small companies, particularly those which partook of the nature of family concerns to the full rigours of our Act, while the achievement of the wider purposes underlying it would be rendered much easier if the Administration could concentrate on companies in which the public interest is large and significant.

5.2. As is well known, the present classification of companies into private limited and public limited is based essentially on the categorisation adopted and followed in successive English Companies Act since 1907. At an earlier stage, our Indian Act merely followed this categorisation. In 1960 a new category of "deemed public" companies was introduced in our Act of 1956 on the recommendations of the Companies Act (Amendment) Committee, 1957. Although the amendment was to some extent influenced by the ideas underlying the English Act of 1948, the refinements introduced in that Act were not fully adopted. The realities of company practice which promoted this amendment have been well-expressed in the following observations of the Companies Act (Amendment) Committee, 1957:—

> "Private companies are exempted from the operation of several sections of the Act and enjoy certain privileges, principally on the ground that they are family concerns in which the public is not directly interested. It is, however, well-known that there are many private companies with large capital doing extensive business and controlling a number of public companies. This is made possible because funds of other companies, public and private are invested in such private companies. As public money is invested in such companies, there is no reason for treating such companies as private companies. The problem of private companies has always been some what difficult. On the one hand, there are genuine private companies which are nothing but glorified partnerships and, on the other, there are

private companies whose operations, financial and industrial, as far wider than those of many public companies. To meet this problem, the Cohen Committee created the category of exempted private companies, but the relevant provisions in the English Act are very complicated. It was strongly urged upon us that the several exemptions granted to and the privileges enjoyed by private companies may cause hardship to genuine small private companies. At the same time, there is no doubt that private companies, which employ public money directly or indirectly to a considerable extent, should be subject to the same restrictions and limitations as to disclose and otherwise as apply to public companies. We, therefore, recommend that a proviso be added to section 3(1)(iv) in these terms:"

"Provided, however, that any private company in which shares to the extent of 25 per cent or more of the paid up capital are held by one or more companies, public or private, shall be deemed to be public company."

5.3. This new category of companies was described as "deemed public" companies in terms of a new section introduced in the Amended Act of 1960 by section 43A of the present Act.

5.4. To cut short the detailed provisions of the Act, it may be stated that, broadly speaking, our Companies Act, 1956, provides for, viz.,

(i) private companies properly so-called;

(ii) private companies which are subsidiaries of public companies. They are subject to the same provisions of the Act as public companies;

(iii) private companies which are "deemed" to be public companies; and

(iv) public companies properly so called.

5.5. This categorisation of companies is, however, still unsatisfactory and involves many anomalies. According to the existing definition, a company will be deemed to be a private company (a) if its membership is limited to 50; (b) its articles restrict the right to transfer its shares; and (c) its articles prohibit an invitation to the public to subscribe for any shares in or debentures of the company. And yet, the size of such a company and its scale of operations may be so large, the impact it makes on large sections of the community may be so heavy and its affiliations to and dependence on other public institutions, financial or otherwise, may be so close and wide-spread, that it would be

as anomalous to exclude a company of this type from the scope of the Companies Act as it would be to leave out any large public company. On the other hand, a public company incorporated as such under the Act, the articles of which do not limit the number of its members to 50 or restrict its rights to transfer its shares and whose size and operations may have very little impact on any section of the public, would be subject to all provisions of the Act ordinarily applicable to public companies although *prima facie* very little public purpose would be served by attempting to regulate its activities as elaborately as in the case of really large public companies. The consensus of views expressed by the witnesses who were examined by us as well as the trend of thinking in this subject in many other advanced countries of the Western World suggest a more rational categorisation of companies based on significant measurable criteria for assessing their public importance or on the impact which they make on the public interest likely to be affected by their working. We have given considerable thought to this subject and have also studied the relevant statistics on this subject. In our view, the advantages of corporate personality and limited liability which were historically extended to private companies properly so called, should be confined to only such small companies as are either in the nature of family concerns or the operations of which are so limited it that they hardly make much impact on interests other than those of their members or their creditors. The definition of a private company should not hinge only on the number of members or on the restrictions imposed by its articles on the transfer of its shares or debentures.

We, therefore, recommend that the present definition of a private company contained in the Companies Act, 1956, should be amended and a private company properly so called should be defined as a company which—

(i) restricts the right to transfer shares;

(ii) limits the number of its members to 50 excluding employees;

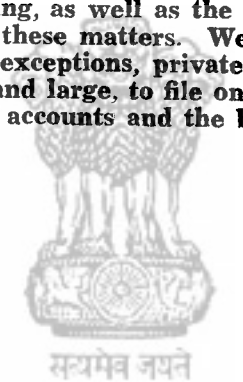
(iii) prohibits any invitation to the public to subscribe for any shares in or any debenturs of the company; and also

(iv) restrict its borrowings from the public and from financial institutions other than banks set up under statutes or under the authority of the Central or State Governments or from any other public company, not being a banking company, to 50 per cent of its paid-up capital.

5.6. If private companies are re-defined on these lines and if they are relieved of the necessity of complying with several restrictive provisions of the Companies Act, the growth of such companies will be facilitated and it may be possible to extend the

benefits of limited liability to enterprises in rural and other relatively backward areas. Further, this amendment will enable the Administration at different levels to concentrate primarily on these companies where the public interest (i.e. the interest of other sections of the community, besides the interests of shareholders and creditors) is involved. Relatively small businessmen, some of whom now complain of the onerousness of the present Companies Act and its requirements, will be excluded from the major restrictive provisions of the Act.

We suggest that the Department may scrutinies the list of the returns which private companies are required to file as well as many of the formal provisions of the Act applicable to them with a view to limiting the requirements of the law applicable to them to a minimum. In particular, we suggest that they should be exempted from complying with Section 314 and these sections which require the passing of special resolutions in general meeting, as well as the filing of the returns pertaining to these matters. We are of the view that with limited exceptions, private companies should be required, by and large, to file only the annual returns, profit and loss accounts and the balance-sheets.



CHAPTER VI

Structure and Organisation of Company Management

The decision making process in companies is necessarily at the centre of any discussion of company management and company practice as well as of the procedural matters relating to the working of business undertakings organised and carried on in the company form. It is, therefore, not surprising that a very large volume of evidence that we recorded was concerned directly or indirectly with the problems of management irrespective of the fact whether the companies were managed by Managing Agents, Managing Directors or Managers. It is only in recent years that the fundamental importance and significance of management in corporate enterprise whether in the capitalistic or in the socialistic countries has been fully recognised. This recognition has led to a noticeable shift in discussions and studies on the subject of joint stock enterprises from the problems of ownership to those of management. In the Western countries a very large volume of literature on the pattern of company management, the system of inter-relations and inter-communications between its organs at different levels and the connected problems of management development including those of the basic qualifications, education and training of company managers has grown up over the last two decades. In our country also some progress has been made with similar studies since the Companies Act, 1956, was enacted. The new awareness of the multiple responsibilities of management in the development of corporate enterprise is slowly emerging *pari passu* with gradual replacement of the family or private business of a few by the large limited company as the dominant form of business enterprise in the country. The concept of the social responsibilities of bnsiness is receiving increasing recognition, as the seminars and conferences on the subject in Delhi, Calcutta and Bombay have already testified. But the law relating to the form, structure and functions of management remains *basically* what it was a generation ago. The Companies Act, 1956 for the first time attempted to bring about some changes in the law by super-imposing on the traditional legal concepts a system of partial social control in the public interest. These innovations are, however, still regarded in some quarters in this country as constituting an external superstructure hanging loosely on the traditional frame of company law and have yet to be fully assimilated into the traditional structure of the law and to vitalise its working principles.

6.2. The responsibilities of management in the complex economic and business life of any modern community, as we have

already indicated, are manifold, viz., to the enterprise, to its shareholders, its creditors, its workers as well as to its customers and the community. It is the task of management to reconcile these separate and sometimes conflicting duties. As the Declaration adopted at the first International Seminar on the social responsibilities held on an all-India basis in Delhi in 1965, asserted, "Each of these parties interested in an enterprise has only a sectional interest in it; it is only the management entrusted with its governance which has the overall responsibility for its success and growth." In this sense if the management has to take a particular view of its obligations it must free itself from widespread dependence on any single interest and must deem itself not merely to be the servant of any one or more groups but develop creative powers of initiation and innovation. How these powers are used depends essentially on the prevailing philosophy of management and the convictions and capacities of managers.

It is for this reason that we consider it very important that the law relating to the organisation, the structure and the powers and duties of management of companies should be such as would enable management to discharge their responsibilities. The predominant form of management in the corporate sector of this country in terms of corporate assets was till lately represented by the Managing Agency System. With the rapidly declining importance of the system, it will be necessary to strengthen alternative forms of management through Boards and Managing Directors and to develop in the top managers those capacities for initiation and promotion of enterprises to which we have referred earlier.

At the same time the economic and social requirements of modern business will need a forum where the Managers of the future could have them sorted out and integrated, in the overall interest of all the parties participating in an enterprise.

6.3. In this view of the added responsibilities of management in the coming years and the additional burden which will be inevitably thrown on it in the wake of the disappearance of the Managing Agency System, we considered whether it might not be advantageous to provide in our Indian law for a modified pattern of the two-tier system of management originally set up in Germany and since adopted in several countries of the European Community. The provisions of West German laws in this respect envisage a form of dual management control in order to safeguard effectively the interest of shareholders, creditors and also to infuse Public confidence in the conduct of the business of companies. This object is sought to be achieved by the statutory recognition of two boards of management, viz., (i) supervisory board (*Aufsichstrat*) and (ii) Management Board (*Vorstand*) Historically, the *Aufsichstrat*

was designed as an institutional device to provide more effective representation for the interests of shareholders in decisions taken by the management of public companies. Later the *Aufsichstrat* developed into a broad forum where other interests like the employees also were represented. The *Vorstand* on the other hand consists of Executive Directors who are incharge of the day-to-day management in the enterprise. In this country the two-tier German system has been hitherto linked up with the important but difficult issue of employees' or workers' representation in the management of business. The theoretical case for a two-tier system of management does not, however, necessarily rest on arguments favouring the representation of the workers' interest on the policy forum. Having regard to the manner in which modern large scale business is carried on, it has been increasingly felt in recent years that shareholders and the other interests involved in company affairs should have as their watch dog a more compact and competent agency, capable of effective action than the annual shareholders' meeting. The task proposed to be assigned to such an agency, in contemporary western literature is that it should, in particular, keep an eye on those aspects of company management which cannot be easily understood from a set of actual accounts, nor even from the report of any efficiency or social audit. Indeed the argument of those who advocate this form of management is that a supervisory board should be constituted as standing watch dog on behalf of shareholders and the other interests connected with an enterprise, and should be distinct from the normal Executive Board. It appears that this line of argument has proved convincing in an increasing number of Western countries as, for example, in Holland and Belgium which seem likely to adopt the German pattern of two-tiers in the near future. French Companies Act of 1966 also introduced this as an alternative constitutional pattern for company management in that country. In the Indian context an appropriate modified version of the two-tier system would be to provide for a supervisory board consisting of representatives of shareholders, the top and middle management, the workers and the public, and its functions would have to be limited to those matters which are now the concern of composite boards, consisting of inside as well as outside Directors, under the Indian and British systems of company management. The *Vorstand* on the other hand would correspond to the closely organised Executive Board consisting wholly of inside employees Directors.

6.4. A logical corollary of this type of set up would be the institution of collegiate or plural executives rather than the familiar one man executive as represented by the Managing Director of a typical Indian or British company. A good deal of discussion has been taking place in the Western countries on the relative merits of the collegiate vs. individual Chief Executive. This issue will become increasingly important also

in the Indian context after the abolition of the Managing Agency System, which, in a sense, provided a crude type of collegiate Chief Executive, although in the great majority of cases the persons constituting the Managing Agency firm or company were either related to each other or belonged to a narrow circle of business friends or to families connected by blood relationship or business partnership.

6.5. We have given a good deal of thought to these proposals, particularly because we feel that the managerial problems thrown up by the eventual disappearance of the Managing Agency system in this country not only call for a net-work of consultative, advisory and financial institutions, but also for a good deal of constructive thinking on the appropriate management structure for large companies in future.

> **In course of our enquiry we were told that many companies were already unobtrusively moving towards the type of management set-up which distinguishes between the supervisory and the management functions. We do not, however, think that the time is yet ripe for writing into our company law any specific provisions on this subject. Instead, we suggest that the developments in the wake of the abolition of the Managing Agency System should be carefully watched and studied. Meanwhile, we suggest that, in their own interest, the business leaders should consider whether it would not be advantageous to encourage the growth of an informal type of collegiate management under the broad supervision and control of composite boards of directors. We have reason to believe that if Senior Executives of companies who have the power to take subordinate decisions could be given access to the management board, and could participate on an equal footing with the top management in major decision-making, the efficiency, quality and the harmony of management would considerably increase.**

It has been aptly said that "the middle class of proprietors stamped their outlook on the first generation of the Industrial Revolution, and the traditional labour movement has made its mark on the generations which have followed. The new middle class of middle managers, technicians and professional men looks like being distinctive of the next phase of advanced industrialism." The management structure of companies must increasingly take notice of this likely development in the future, and business leadership must concern itself more and more with the patterns of management that could be appropriate to these developments.

6.6. Pending these developments, we consider that an appropriate management structure for public companies

would be proided by one or more full-time managing directors or whole-time working directors, or whole-time managers who must have seats on the Boards of these companies. Following the abolition of the Managing Agency System, we should like the law to provide compulsorily for at least one Managing Director or one whole-time Director, or a Manager with a seat on the Board of every public company.

The Companies Act, 1956, already provides that no one can be appointed to be a Managing Director for more than two public companies except with the approval of the Central Government. We consider that this prohibition should also extend to private companies i.e., no one who is a Managing Director of a public company shall be appointed Managing Director of four companies in all including private companies.

6.7. In the context of the reorganisation of the management structure of companies in future we have also to consider the question of the participation of workers' representatives in the management of companies. Although a few witnesses raised this issue before us on the analogy of the provisions relating to workers' representation on the German Supervisory Boards, we felt that the time had not yet arrived for any such provision in our law. Nor did the demand for such representation on the Boards of companies appear to us to be particularly strong or insistant.

6.8. We have also considered whether there is a case for a statutory provision for workers' representation at a lower level in the management of companies, specially in regard to matters which directly impinge on or affect the interests or the duties and responsibilities of workers. The effectiveness of employees representation on the Supervisory Boards of German companies owed not a little to the part played by the network of employee representation through trade unions and statutory work councils both at national and enterprise or plan level.

We are inclined to take the view that it is only after further improvements have been made in workers' right and more systematic and comprehensive use has been made of a wide range of joint determination within an enterprise in its day-to-day activities that statutory representation of workers in the management of companies whether at the top (Board), middle (Executive management) or lower (Shop-floor) levels can be considered.

Much remains to be done to strengthen and to give a clearer definition by elaborate law and collective arrangements to the respective duties and responsibilities of the management and the employees. Before any attempt is made to provide for the statutory representation of workers at any desired level in company management, efforts should be made to improve the education and training of workers for some of the elementary tasks of management.

For all these reasons, we do not consider that it is necessary at present to provide in the Companies Act compulsory representation of workers at any level of management. But it is our hope that it may be possible for the management of companies increasingly to associate the workers' representatives, particlarly at the shop-floor level, so that all management decisions that affect the interest of workers can be taken in the full light of the discussions with workers' representatives.

6.9. It remains to examine the question of the representation of the public, including consumers, on the Boards of companies. This subject has been debated off and on in this country and has been under detailed study in the Western countries in recent years. Our Companies Act already empowers Government to nominate not more than two persons, who may or may not be members of a company, as its Directors for a period not exceeding three years at a time, if Government is satisfied that such appointment is necessary either in the public interest or to prevent a company from being conducted in a manner which is prejudicial to its interests or is oppressive to any of its members.

We are not, however, sure whether the provisions of the law should also provide for compulsory representation of the consumers or of the general public on the Boards of sompanies.

Even if this suggestion is accepted in principle, difficulties are likely to arise as to the methods of election or selection of representatives of consumers and the general public. What should be the number of such directors who are to be appointed? If only one or two directors are to be appointed, to what extent are they likely to be effective? How one is to ensure that only men of integrity and independence of character are appointed as such Directors?

On the whole, we are inclined to the view that unless further discussion and debate has clarified many of these issues, it is not necessary to provide in the law for any such representation.

6.10. There is another major issue relating to the management structure of Companies which was brought to our notice, specially by the shareholders' representatives. It concerns the question of minority representation on the management of companies. It was conceded that the existing provisions in the company law empowering the minority to ask for enquiry or investigation or for a change in the management of the companies in the event of gross mis-management or oppression to a minority did recognise the latter's rights. It was, however, contended that more automatic and expeditious action was needed in many cases. Suggestions were, therefore, made that the existing provisions of the law relating to proportional representation on the management of companies should be made compulsory in those cases where a minority of the shareholders demanded election of Directors on this basis. It was argued that this system of election of Directors ensured an automatic internal check on the management of companies which was preferable to the type of external intervention which our law now provided. In support of this claim it was pointed out that several states in the U.S.A. Provided for such election (through the system of cumulative voting) in their corporation laws, and the experience in that country was that this requisement did not lead to any serious undesirable results in company management or practice.

While we are in sympathy with the claim that the minority of shareholders should be adequately protected through representation on the management of companies, we are somewhat hesitant about recommending a compulsory system of proportional representation for all or even selection groups of companies. Our hesitation arises from the fact that the present provisions of section 265 of the Act which gives an option to a company to adopt proportional representation for the appointment of Directors has hardly been used even in those cases where several groups of shareholders constituted substantial minority. Nor are we quite sure if the complications involved in working out a system of proportional representation would not seriously prejudice the relations between the Directors representing different groups among shareholders and the company. Indeed the entire subject of proportional representation in the context of the provisions of 265 requires further detailed study, and we suggest that the Government should initiate this study immediately, so that when the Companies Act, 1956, is comprehensively amended in future, a further close look may be given to the present virtually inoperative section 265 of the Act. In this connection we should like Government to examine a specific suggestion made to us by some witnesses, viz., that where a substantial minority of shareholders ask for the appointment of a

Director in addition to those who are already on the Board it should be necessary for a company to appoint him to the Board, notwithstanding anything in the Articles of the company or the provisions of the Act relating to the election of Directors.

The suggestion is not free from difficulty, and it may also be necessary to hedge the right of a minority group, in order to ensure that a provision of this type does not encourage the staking of claims by groups of shareholders or encourage competitive bidding for votes by them.

6.11. In the context of the need for strengthening the rights of minority shareholders, a suggestion was made for conferring the right to speak on the proxies of shareholders. At present section 176 of the Companies Act, 1956, denies any such right to a proxy, who may, however, attend any meeting of the company and vote for his principal.

We feel that the time has come when the right to speak should be extended to a proxy.

Fear has been expressed in some quarters that this right might be abused and encouraged the growth of a class of 'professional' proxies. We do not share these misgivings. On the contrary we feel that if this right was extended to proxies, it may well enliven the annual general meetings of companies, and elicit a good deal of information about its working which shareholders may reasonably expect but which at present is not available to them in a form which is easily understood by them. In the case of companies with widely dispersed shareholdings, the absence of this right virtually deprives shareholders who are now prevented from attending the annual general meeting of a company by the high cost of travel from exercising their rights as its members.

6.12. There is another important suggestion directly concerning the management structure of companies which was made to us at all the important commercial centres that we visited. Since the Companies Act, 1956, was enacted, many of the larger companies have considered it necessary to appoint qualified company secretaries, to look after the detailed requirements of the law on behalf of the management. This practice has slowly grown over the last few years, and received a fillip from the action which was taken by Government after 1956 to organise a system of examination for Company Secretaries on an all-India basis at several selected centres in the country. We understand that the courses and syllabi of studies for this examination are prescribed in consultation with the representatives of the professions concerned and successful students are sent out for six months' practical training in recognised companies, and a fortnight's training in a Registrar's office. After this training, we

learn they are awarded diplomas. Several competent witnesses assured us that the standard of this examination was fairly high. In order to give a boost to the profession of Company Secretaries and also to induce a larger number of companies to utilise the services of qualified secretaries, it was pressed upon us by many witnesses, particularly those belonging to the professions connected with company management that the Companies Act should provide compulsorily for the appointment of Secretaries in all public companies. In 1956 when the Act was passed a similar demand had been made in some professional quarters. The view taken by Government at that time was that having regard to the large number of posts that would need to be filled, it would be difficult to ensure the requisite supply of qualified men. Indeed the fear was expressed that if a compulsory provision in the law was made for this purpose, albeit limited to public companies they would in all probability have to be filled up by not properly qualified persons, who could hardly be expected to measure up to their responsibilities. We were given to understand that the position in regard to the supply of qualified men had since improved considerably. Besides, we were told that courses for Company Secretaries' examination were now offered in several well-organised educational institutions, specialising in the training of Company Secretaries and Company Executives in all the leading commercial centres of India.

We are, therefore, of the view that the Companies Act should now provide compulsorily for the appointment of qualified secretaries in the case of all large public companies, say, with a paid up capital of Rs. 50 lakhs or more. We also recommend that suitable qualifications for such Secretaries should be prescribed by Government. They should be such as will include persons who have passed the examination organised by Government on an all-India basis and obtained diplomas from Government and others who have passed recognized academic or professional examinations directly concerned with the management of companies.

CHAPTER VII

Company management in practice—some important problems

Section A

Having considered the problems relating to the structure of company management, we now proceed to consider those provisions of our company law which impinge on the processes of management and the general frame-work of legislative and administrative constraints within which the management of companies is carried on in this country.

7.2. Before, however, we proceed to do so, there is one general observation which we should like to make. No law or administrative policy in itself can do much to develop management potential or to improve the quality of management. The scope of law and sound administrative policy in relation to management is limited to the creation of those conditions under which the right type of top managerial personnel may be recruited, and given those opportunities for the promotion, expansion and development of business enterprises which would ensure that enterprises are carried on honestly, efficiently and with due regard to the interest of those who are directly involved in the enterprise as well as of those who are indirectly affected by their processes and end-results.

7.3. A great deal of discussion has taken place during the last two decades in all industrially advanced countries and more recently in our own about the education and training of the top executives of industry and their specific role in the type of 'participative task leadership' which the top direction of a modern business enterprise requires. The main reason for this approach to modern management is the simple fact that in the top level of any large business undertaking in the present day many different interests have to be reconciled; they are powerfully represented and cannot be over-riden. To integrate these interests and to evolve a synthesised policy which takes notice of all of them, requires a type of 'task leadership' which is very different from the type of single-individual management control with which the business leaders of an earlier generation were familiar. It is only a carefully designed management development policy that can produce this type of leadership. The formulation of such a policy is a task which can be adequately and effectively undertaken only by business leaders with the help of experienced educational planners acquainted with the needs of business. Company Law, as such, can do little to foster such leadership in a positive manner.

7.4. It is, however, the proper province of Company Law and administrative policy concerned with the implementation of such law that, till the right type of business leadership has been built up, the interests of shareholders, employees and the community in the sound management of a business should be safe-guarded against dishonest or amateurish top management. Towards this end law and administrative policy should ensure that this protection is provided, without unduly loading the top management with such internal or external control as inhibit the management's essential freedom to choose and carry out the strategy of the enterprise. The provisions of the Companies Act, 1956, were in a sense in the nature of a holding operation against managerial malpractices and mis-management pending the growth and development of the appropriate managerial conscience. The regulative provisions of the Companies Act, 1956, relating to the appointment and the powers and duties of the directors should be viewed in this light.

7.5. Section 269 of the Companies Act, 1956, requires the previous approval of the Central Government to the appointment of any person, for the first time, as a managing or whole-time director and also to his reappointment as such. It follows that the terms and conditions on which a person can be so appointed or reappointed also needs the approval of the Central Government. Several witnesses complained of the delay in the disposal of individual applications at the headquarters of the Central Government in Delhi and commented on the absence of any firm and consistent principles in regard to these matters. In order to reduce the volume of work and to eliminate the delays which the treatment of individual applications necessarily entails, it was suggested to us that Government should be in a position to indicate in sufficient detail the type of qualifications and experience which they would expect of the managing or whole-time directors of public companies, and should also lay down the broad limits of the remuneration to be given to them, so that in cases where the companies conformed to these requirements, they might be absolved from the necessity of submitting individual applications. We shall revert to the question of the remuneration of managing or whole-time directors again in another section of this chapter. For the present we are concerned with the requirement of the Companies Act relating to the prior approval of Government for the appointment of managing or whole-time directors for the first time. The difficulty of laying down any general principles defining the qualifications and experience needed of managing or whole-time directors is, however, a formidable one, and we agree with the view of the departmental witnesses that it is almost impossible to lay down any positive criteria of fitness such as would eliminate the necessity for individual applications. Obviously neither theoretical or academic qualifications nor age would provide adequate standards ; nor would such qualifications, even if they could be laid down, be appropriate for all types of enterprises. Given the

need for passing judgement on the suitability of managing or whole-time directors in public companies, we see no escape from the procedural requirements of the law.

Nevertheless, we feel that the Administration should be able to lay down, in general terms, the type of individuals, who would *prima facie* be judged unfit for appointment as managing or whole-time directors of public companies, and to make its general policy known to the business community and to the shareholders and others directly concerned with the management of companies. Section 274 of the Act lays down some disqualifications of directors. We suggest that the Administration would consider the feasibility of adding to this list in the light of its administrative policy as regards the appointment and reappointment of managing or whole-time directors. This will be in the nature of a supplementary list of disqualifications intended for the guidance of the business community, although deviations from these further conditions might be considered by the Administration in exceptional cases.

7.6. Under Section 275 of the Companies Act, 1956, no person can be director of more than 20 companies. This number excludes private companies, un-limited companies, associations carrying on business for no profit, and all companies in which an individual is only an alternate director.

Many witnesses who appeared before us considered that this number was unduly large and needed to be reduced to ten in case of public companies and 15 in the aggregate inclusive of private and other companies, but exclusive of associations carrying on business for no profit. We agree with this view and suggest a suitable amendment of the Act in due course.

7.7. Several witnesses also complained of the absence of any provision in the Act relating to the retiring age of the directors. It will be recalled that the Companies Act, 1956, had laid down an age limit for directors, but the Amending Act of 1965 deleted the relevant section. We have not been able to appreciate the reason for this official amendment. On the contrary we consider that, in line with the thinking implicit in several other statutes which prescribe suitable age limits for incumbents of high offices, a suitable retiring age for directors of public companies should also be laid down in the Companies Act. We, therefore, feel that the statute should be suitably amended in due course so as to provide for a suitable retiring age of directors.

In our view no one who has attained the age of seventy should be permitted to continue as a director, and no deviations from this rule should be permitted.

7.8. A suggestion was made to us by one or two important witnesses that it would be a healthy practice in company management if managing or whole-time directors and other full-time executives of companies were prohibited from becoming part-time directors of other public companies. The argument underlying this suggestion was that the object underlying the provisions of the Companies Act unler which no person could become managing or whole-time director of more than two companies could be largely frustrated if he was permitted to hold a large number of part-time directorships in several other public companies to the direction of which he could hardly be expected to contribute much. We were advised that this practice arose from the fact that many companies were anxious to have on their Boards a few well-known names and not because of the time or thought which the selected individuals could possibly devote to the policies or programmes of the companies. This we consider an undesirable practice.

We, therefore, recommend that a suitable provision in the Companies Act should be made either to do away with this practice or at least to mitigate its evils by limiting the number of ordinary directorships which a managing or whole-time director of a public company can hold to not more than two or three. The fees received by such a director for attending the Board meetings of the other companies should, we consider, be surrendered on suitable basis to the company or companies of which he may be a managing or whole-time director.

7.9. There is one more important point bearing on powers and duties of directors on which we should like to comment in this context. We do so because in our judgment this also affects their capacity for good to the companies with which they are connected and also involves them in needless controversy. We refer to the provisions of section 293A of the Companies Act which empowers the directors of a public company to contribute to charitable and other funds not directly related to the business of the company or to the welfare of its business, any amount not exceeding Rs. 25,000 or 5 per cent of the company's average net profits, whichever is greater. We understand that Government have recently taken a tentative decision to prohibit contributions to political parties or for any political purpose. If this is so, we endorse this decision, although we recognise that contributions for this purpose could and perhaps would still be made deviously out of a company's funds, which may

not be easy to detect from the company's published accounts. This is, however, no argument for the law to continue to countenance the present practice. We would, however, go a little further in this connection.

While we agree that suitable amendments of the existing laws should be made to prohibit contributions to political* parties or for political purposes out of company funds, we do not consider that similar curbs on the use of company funds for charitable purposes, which are duly recognised as such, in the revenue and other laws of the country, are called for except that such contributions should be disclosed in the company's published annual accounts.

SECTION B.

7.10. We now come to the difficult and somewhat controversial issue of the direct control which Government exercises over the remuneration of directors in all public companies. No other issue arising out of the enforcement of the Companies Act has evoked so much comment as the provisions of the Act relating to this subject, nor do the other restrictive provisions of the Act seem to have caused so much irritation and annoyance to the management of companies as this section of the Act has apparently done. This issue has been the subject of a continuous debate between the Administration and company management ever since the Companies Act, 1956, came into force, and the decisions of Government on individual cases still attract comments. We, therefore, consider it desirable to preface our observations and recommendations with a brief recital of the evolution of Government policy on this subject as we have understood it.

7.11. In the early years of the implementation of the Act, between 1956 and 1960, Government policy on this subject was concerned with laying down elaborate guidelines, within the broad frame of the statutory provisions, for the examination of individual cases by the officers of the Department concerned. In this task the Administration was assisted by the Company Law Advisory Commission. The intention was that individual applications for the fixation of remuneration or for increasing the remuneration of managing agents or managing directors should be examined in the light of the prescribed scales, which

*Two of our members, Shri H. P. Nanda and Shri M. V. Venkataraman however, expressed the view that the existing provisions of the Companies Act relating to contributions to political parties or for political purposes should remain unchanged pending a decision on the issue of policy by Parliament in due course.

purported to take into account all important relevant factors which, in the judgment of the Administration had a bearing on the remuneration of the top management of companies. This meant that, in practice, within the statutory limits of remuneration laid down in the Act, certain administrative ceilings were also, in effect, prescribed in the light of the maxima considered by the Administration to be fair and reasonable. The factors which were taken into account in prescribing the administrative ceilings were explained from time to time and were also reproduced in the Annual Reports on the Administration and Working of the Companies Act which were required to be placed before Parliament. Some witnesses told us that at a later date the variations from the prescribed norms were not infrequent, and where the Administration sanctioned level of remuneration not strictly in accord with the scales laid by themselves, no attempt was made to explain adequately the reasons for the deviations. Apparently this has caused considerable dissatisfaction with the manner in which actual levels of remuneration have been fixed in individual cases, within the administrative ceilings prescribed by the Administration, and charges of discriminatory treatment have been made from time to time.

7.12. Perhaps this impression was in part due to the fact that from the end of 1963 onwards the exercise of the discretionary authority vested in the Administration on this subject was unaided by the considered advice of a duly constituted authority outside the Administration. Till 1963, the Administration had the benefit of recommendations from a statutory Company Law Advisory Commission set up under section 410 of the Companies Act. This provided a built-in institutional check on decisions taken by the Department concerned. The Amendment Act of 1963 abolished the Company Law Advisory Commission. We shall consider in another chapter of this Report some safeguards against possible discrimination in the use of the discretionary authority under the Companies Act vested in the Administration. Meanwhile, we refer to this matter only as a preliminary to our examination of some suggestions which were made by witnesses for restricting the scope of individual judgement in decisions relating to managerial remuneration.

7.13. The administrative ceilings prescribed by Government in the case of remuneration to managing agents have hitherto been on the following sliding scales :—

10 per cent on the 1st ten lakhs of net profits.
9 per cent on the next ten lakhs of net profits.
8 per cent on the next ten lakhs of net profits.
7 per cent on the next ten lakhs of net profits.
6 per cent on the next ten lakhs of net profits.
5½ per cent on the next 25 lakhs of net profits.
5 per cent on the next 25 lakhs of net profits.
4 per cent on any sum over Rs. 1 crore.

7.14 The circumstances in which in consultation with the then statutory Asvisory Commission, Government consider it necessary to prescribe the above sliding scales were explained in the Fourth Annual Report on the Working and Administration of the Companies Act, 1956, for the year ended 31st March, 1960 @ and also in the Report of the Company Law Advisory Commission for the year ended 31st March, 1960*. The implications of the sliding scale and its impact on the earnings of managing agents were set out at some length in the former Report. It was also at the same time emphasised that the sliding scale was intended to be used as a guide by the Company Law Advisory Commission and the Department and deviations from the scale would be permissible in individual cases, if their special circumstances justified the payment of remuneration in excess of the amounts admissible under the scale. Similarly, another sliding scale of remuneration was laid down for Secretaries and Treasurers within the statutory limits of their remuneration laid down in the Act. We do not propose to go further into the principles followed by the Administration in approving of remuneration payable to Managing Agents and Secretaries and Treasurers, because we understand that Government have already taken a decision as to the abolition of the managing agency system in the near future, and we presume that the institution of Secretaries and Treasurers would, for similar reasons, be also abolished at the same time.

The institution of Secretaries and Treasurers in the form in which it was conceived and later embodied in the Companies Act, 1956, was intended to provide for a competent body of corporate managers in place of the traditional system of management by managing agents. These corporate managers were supposed to be professionally trained individuals who, by reason of their familiarity with the techniques of management and financing and the technologies connected with the manufacture or production of goods and services, could be expected to make available to the joint stock companies under their charge the expertise necessary for large scale production and management, without exercising the typpe of deletorious economic power or influence over them such as the average managing agents did. Speaking in support of this new institution in the Companies Act, 1956, the then Finance Minister who was in charge of the Companies Bill, 1953, observed as follows :—

> ..... **In its essence, this institution seems to be nothing but a form of management through corporate managers. If I may say so, that Joint Committee**

@Vide paras 77 to 82 of the Fourth Annual Report on the Working of Company Law Admn. Department.

*Vide para 6 of the Annual Report of the Company Law Advisory Commission.

have made a valuable contribution to the growth and development of an alternative form of management by their proposal to recognise this kind of management formally in the Companies Act. There are, of course, views both for and against this. But, if Hon. Members will carefully read the provisions of clauses 378 to 383 which deal with Secretaries and Treasurers, they will have no difficulty in appreciating the object underlying them. While the Joint Committee was anxious to prevent the concentration of economic power in the hands of a few managing agency houses with long established tie-ups with financial institutions like banks and insurance companies, it was equally anxious to ensure that no sudden vacuum was created in the organisation of trade and industry by a possible decline or disappearance of the managing agency system in some sectors by 1960. They recognise that the Secretaries and Treasurers would have no economic power. That is to say, it would be the managing agency system without its teeth. Therefore, they were concerned to develop a form of a management which would preserve all that was good, as far instance, the pooling of technical competence, in the institution of managing agents by denuding it of its power to dominate the affairs of the managed companies. Secretaries and Treasurers would not be entitled by virtue of their agreements alone to have any representation on the Board of Directors. For myself, I do not see that there is any inconsistency between this anxiety to prevent the concentration of economic power and at the same time to try to retain for trade and industry those benefits of large scale and expert management and supervision which at least the best among the managing agency houses have always conferred on the companies managed by them*.

Unfortunately, in the event, this expectation has been almost wholly belied. Secretaries and Treasurers of the typo visualised in 1955-56 have hardly grown up so far, and the institution has been used mostly as an alternative device for running the companies by the existing managing agents under a different name. In the result, several provisions of the Act relating to managing agents have been by-passed and the objects underlying them have been partially defeated. It does not, therefore, seem to be of any use in persisting with the experiment begun in 1956.

7.15. In regard to the remuneration of managing or whole-time directors, an administrative ceiling of Rs. 1,20,000 per

***Vide Lok Sabha, 10.8.1955 : Debates, Vol. V, No. 13.**

annum within the statutory limit of 5 per cent of the net profits of a company in the case of such director and 10 per cent in the case of more than one, was laid down soon after the Act, 1956 came into force. This ceiling was inclusive of the commission on profits, if any, but exclusive of the fringe benefits sanctioned by the company. The factors which the then Company Law Advisory Commission and Government took into account were explained in the Annual Reports of the Department of Company Law Administration and the Company Law Advisory Commission in the earlier years. Subsequently this administrative ceiling was raised to Rs. 1,80,000 per annum again exclusive of the perquisites ordinarily paid by the companies. Here again, the administrative ceiling laid down by Government was not rigid limit and deviations were permitted from it in some classes of companies and even in individual cases where, in the opinion of Government, circumstances justified such payment in excess of this administrative ceiling.

7.16. Alongside of the fixation of administrative ceilings in the manner indicated above, administrative floors were also laid down, providing for a scale of minimum remuneration in the case of managing agents (including secretaries and treasurers) and mangaing or whole-time directors. This administrative floor extended from Rs. 7,500 per annum to Rs. 50,000 per annum which was the maximum of the minimum remuneration payable under the statute. As in the case of the administrative ceilings on remuneration, the floor scales could also be exceeded, for special reasons, with the approval of Government.

7.17. The principal criticisms against this system of direct control over remuneration voiced before us were that—

(a) in fixing the remuneration in individual cases, the administrative judgment of the officers had been substituted for the judgment of the management or the shareholders ;

(b) while the elaborate system of direct control provided for sufficient flexibility in its operation, it kept the management in doubt as to what the decision of the Administration would be in individual cases. In other words, the second criticism was not so much against rigidity in the application of the law to individual cases as against its uncertainty.

7.18. Any system of direct control involves an exercise of judgment on the part of controllers. While we appreciate the argument that in principle such control should be selected and limited to cases where other forms of control capable of achieving the same results are not likely to be effective, we do not think that, having regard to the policy underlying the scheme

of direct control over managerial remuneration, and the circumstances in which this policy was formulated more than a decade ago, any other form of control over managerial remuneration based only on the judgment of the management and the shareholders would have been an adequate substitute. The discipline imposed on company management by the present system of direct control over managerial remuneration during the last 10 to 12 years may. however, be expected to have secured the acceptance of other norms in this area. We further assume that the proposed abolition of the managing agency system will not encourage the abrupt marking of the current levels of remuneration of the Chief Executives of companies. If these presumptions are correct, it may be worthwhile to consider whether some relaxations in the operation of the existing control would not be desirable. This might have the effect of reducing the sense of uncertainty which acts as a psychological irritant to those business executives who are affected by the provisions of the Act. To the extent that avoidable tensions in the managerial field can be removed without appreciable damage to the basic policies underlying the system of control over managerial remuneration, it may be worthwhile to give the management and the shareholders a larger say in the fixation of the remuneration of their chief executives.

7.19. With regard to the minimum managerial remuneration admissible under section 198 of the Act, several witnesses brought to our notice the hardship caused by the maximum of such minimum remuneration laid down in this Act. It was complained that Government was reluctant to sanction a reasonable minimum remuneration for the Chief Executive of a company for the duration of his term of office irrespective of the fortunes of the company and that this reluctance was a source of grievance to company management. We understood that a provisional minimum remuneration for a short period while the company earned no profits or its profits were inadequate was ordinarily sanctioned, and the company was asked to approach Government again as soon as it had begun to earn profits. In the case of companies managed by managing agency firms or companies, this was perhaps a suitable procedure to follow, when the managing agency system was still the dominant form of management. In the case of professional managing directors or whole-time directors, however, this type of provisional payment may turn out to be a real deterrent.

It seems to us, therefore, that in such cases it will be more appropriate to fix a suitable remuneration for the Chief Executive of a company after taking into consideration all relevant factors, in relation to its size and the nature of its business and the qualifications, experience and background of the selected Chief Executive

and, of course, with due regard to the company's profits earning capacity for the entire period of his first appointment and to treat this as minimum remuneration admissible to him under section 198 of the Companies Act.

The provisions of this section permit this course to be followed in all those cases where a monthly payment is proposed to be made. As a safeguard, Government may reserve the right to call for regular periodical information about the performance of the company at any time, and indeed as often as it considers necessary to do so, during the period of the first appointment of the Chief Executive in order to satisfy itself that the remuneration sanctioned for him is justified.

7.20. Another problem connected with managerial remuneration, created in the wane of the recent depression in several industries in this country, was brought to our notice. We were informed that the present practice was to lay down only the maximum remuneration which a company could pay to its Chief Executive within the limits of the statutory provisions. It was pointed out to us that in several cases, as the companies had ceased to earn adequate profits the Chief Executives concerned were unable to earn the remuneration sanctioned by the Department. Consequently the companies had to approach the Department again with the request to fix a corresponding minimum remuneration for their Chief Executive, equivalent to the remuneration which had been sanctioned to him. This is a problem which companies face largely because of the fluctuations in their earning capacity, which appear to have been accentuated by the present recession in some industries. If the fall in the profits of a company is expected to be of short duration, we do not see why a Chief Executive should not continue to draw the same remuneration which had been sanctioned for him in a relatively good year.

7.21. Difficulty may, however, arise if the fall in profits continues for several years, and particularly in the case of companies which are unlikely to recover their profits-earning capacity on account of basic shifts in the structure of the economy affecting their markets. In such cases, it may not be obviously in the interest of the companies or of the economy as such that the Chief Executives continue to be paid at levels which foreseeable prospects of the companies 'concerned' do not justify. In such cases an appropriate balance of relative equities would seem to suggest that the minimum remuneration of the Chief Executive should not continue to be fixed at the level of the remuneration originally sanctioned for him but at a lower level which the companies concerned could bear. At the same time we consider that such

adjustments in the remuneration of the Chief Executive should not be attempted on the basis of only the annual fluctuations in a company's profits but when the profits showed no prospect of improvement even after a period of two to three years.

7.22. Our broad conclusions on this difficult question of control over managerial remuneration are, therefore, as follows :—

(i) Within the limits of the statutory ceilings prescribed for such remuneration in sections 198, 310, 326, etc. of the Companies Act, 1956 and subject to the maximum administrative ceiling laid down by Government, the shareholders should be free to fix the remuneration of the Chief Executive of a company at an appropriate level after taking into account all the relevant factors which are now considered by Government in fixing the remuneration payable to them. The decision of the shareholders should be taken by a special resolution at a meeting;

(ii) this decision should be conveyed to Government within a fortnight of the special meeting to be held for this purpose;

(iii) Government should have the right to call for such further information as they wish to have in regard to any such decision and to order any suitable modifications in the proposed remuneration or in the terms and conditions of employment of the Chief Executive of a company, within a period of two months of the receipt of the certified copy of the special resolution passed by the company; if no such information is called for or no objection raised within 60 days the company's proposals would be deemed to have been approved ;

(iv) In regard to minimum remuneration, Government should sanction a reasonable remuneration in the case of salaried employees for the entire period of the first appointment of a Chief Executive, in the case of a new company;

(v) in the case of going concerns, the remuneration duly approved by Government should be deemed to be the minimum remuneration for a period of two to three years at a time. If at the end of this period it is found that the amount of remuneration sanctioned is in excess of the statutory limit, Government should have the right to review the case and to prescribe such other remuneration as may be appropriate to the fortunes of the company. For this purpose suitable guiding

principles should be framed and communicated to the Chambers of Commerce and other trade associations;

(vi) in order to give publicity to the decisions of the Company Law Board on the terms of remuneration approved for managerial personnel, the Board should take steps to publish approved terms in the suitably abridged form in its fortnightly journals where it is already publishing the appointments and re-appointments of managerial personnel.

7.23. We recognise that the relaxation of the administrative practice and procedure which we have recommended may tempt unscrupulous company managements to raise the existing level of their remuneration of fix the initial remuneration in the case of new companies at levels which bear little relation to the earning capacity of the companies concerned. The power which we propose to vest in the Government to call for information about the performance of companies at any time after their managerial remuneration has been fixed, would enable Government to intervene in such cases, if it is reasonably vigilant and makes quick use of the information collected by it. For the rest, we expect the management of companies to use the freedom proposed to be given to them in this field with discrimination and a due sense of responsibility. In any case, if these recommendations lead to widespread abuse of this freedom, it would be open to Government to review the new policy and to take appropriate measures.

7.24 Several witnesses who appeared before the Working Group referred to the provisions of the Companies Act relating to inter-corporate loans and investments. The view was expressed that the limits within with a public company could invest in the shares of another company were unduly restrictive. It was contended that, in the depressed state of the money and capital markets, they deprived newly formed as well as existing companies from drawing on an important source of capital and thereby acted as a disincentive to the formation of capital. Further, complaints were made about the delay in the sanction of inter-company investments beyond the prescribed limits even in cases where such investments were otherwise fully justified. We have had the advantage of a detailed case study on this subject by the Department of Company Affairs, which was good enough to explain to us the guiding principles which had been laid down for the guidance of the departmental officers.

We do not think that the criticisms about the present procedure and practice are fully justified. On the contrary, we consider that the reasons which prompt-

ed the imposition of the present restrictions on inter-company investments still exist, and that, in the circumstances of company management in this country and in order to prevent dissipation of a company's resources ond undue concentration of economic power in a few hands, it is necessary to maintain some curbs on the freedom of management to invest in the shares of other companies.

In this connection our attention has been drawn to the need for encouraging investments in priority industries. We have no doubt that in considering applications for inter-company investments in excess of the limit laid down in section 372 of the Companies Act, the Administration will take due note of the desirability and importance of encouraging investments in such industries provided the management of the companies concerned can be depended upon to make good use of such investments and the resources of the investing company permit of such investments without detriment to its own legitimate needs.

7.25. The present section 372 of the Act provides that the Board of Directors of a company shall be entitled to invest in the shares or debentures of another body corporate upto 10 per cent of the latter's subscribed capital, provided :

(i) the aggregate of such investments made in all such other bodies corporate does not exceed 30 per cent of the subscribed capital of the investing company, and

(ii) the aggregate of such investments in all other bodies corporate in the same group as the investing company does not exceed 20 per cent of the latter's subscribed capital.

The section further provides that these limits can be exceeded by an ordinary resolution of the company, and with the approval of the Central Government. Several types of inter-company investments are excluded from the scope of this section, e.g., (a) investment in rights shares; (b) investment by companies whose business is to invest in other companies; (c) investments by financial institutions duly recognised by Government; (d) investments by holding companies in their subsidiaries, etc. The statistics relating to applications submitted to Government under this section which were placed before us by the Department of Company Affairs shows that in the years 1963-64, 64-65 and 65-66, the average annual rejection of such applications in terms of the amounts involved, was hardly more than Rs. 1 crore as against applications for sanction of the average annual value of about Rs. 10 crores.

We do not, therefore, consider that the operation of the statute has been unduly severe or that the powers conferred on the Central Government have been exercised with undue rigidity. We, further note that since the present provisions were inserted in the Companies Act, 1956, the guiding principles formulated by Government have taken due note of the legitimate needs and requirements of business.

The guiding principles have been also reproduced in the successive Annual Reports of the Working and Administration of the Companies Act and have also otherwise been widely publicised. The procedure laid down for the examination of these cases calls for the submission of several essential documents, e.g., (a) copies of the resolution by the investing company in general meeting; (b) copies of the resolution passed by the Board of Directors of the investee company approving of the investment; (c) copies of the Memoranda and Articles of Association of the companies concerned; (d) copies of the balance sheets of both the investing and the investee companies; (e) copies of prospectuses, if any, issued by the investee companies, etc.

We do not think that the obligation cast on the public companies by this procedure is unduly onerous.

If the affairs of a public company are being managed in a reasonable, systematic and orderly maner, as they should be, there should not be much difficulty in supplying copies of these documents which would have to be maintained by the company in any case, even if it were completely free to invest in other companies. We have considered a suggestion for doing away with the requirement of the Central Government's prior approval if investments in excess of the permissible limits are duly approved by the company at a special meeting.

Those who made this suggestion conceded that the Government might retain the right to call for such information as they might need about such investments at any time within a reasonable period of their having been made, and if as a result of subsequent scrutiny they considered that the 'excess' investment was unjustified, it should have the right to require the company concerned to liquidate this 'excess' investment. We fear that this might prove to be a severe hardship on most companies which had already made such investments, and in some cases might damage their credit.

We do not, therefore, consider that this suggestion would be of any odvantage to the companies.

On the contrary, it might well create problems and difficulties which the present requirement about prior approval of the Central Government avoids.

7.26. The question of inter-corporate loans under section 370 was touched upon by several witnesses in the context of our discussion on inter-corporate investments. Some of them suggested that while there might be good reason for Government to arm itself with powers to regulate inter-corporate investments, inter-corporate loans belonged to a different category of financial transactions which did not require the same measure of oversight. In this view, it was claimed that it was not necessary for Government to intervene in cases where the aggregate of loans to all bodies corporate exceeded 30 per cent of the aggregate of the subscribed capital of the lending company and its free reserves. We have carefully looked into the provisions of this Section as it was amended by the Act of 1965. The amended provisions of this Section were brought into force only with effect from April 1, 1967, the interval of time being presumably intended to give an opportunity to the company managements to adjust their inter-company loans so as to bring them within the latest requirements of the law. We understand that the Department of Company Affairs has not yet formulated any firm guiding principles for the use of its officers in implementing the provisions of this section and that they are expected to follow the broad principles laid down some years ago about the grant of loans by public companies to their Directors or to such companies in which their Directors were interested.

In the case of inter-corporate loans we suggest that the criteria to be taken into account by the Administration in dealing with applications under section 370 of the Companies Act should include (i) the financial position of the applicant company; (ii) the financial position of the borrowing company; (iii) the security offered; (iv) the rate of interest on the loans; (v) the terms and conditions for the repayment of the loans; (vi) the purpose for which the loan was proposed to be given; and (vii) the present position of the loans and investment portfolios of both the lending and the borrowing companies.

Although this section is relatively new and the business community has not yet had time to form its views on its working. We do not think that the enforcement of this section will cause any more difficulty or complication than the administration of section 372 of the Act now presents.. Nor do we think the requirements of this section throw any undue burden on the management of companies. As we read the provisions of the two sections viz. 370 & 372, a company would be virtually free to utilise its funds aggregating to about 60 per cent of its subscribed capital, if it has any free reserves.

In view of this liberal margin on which companies will have the freedom to operate, we do not consider that

there is room for any legitimate apprehension about the effects of these provisions on company practice or on the orderly growth and expansion of corporate business.

7.27. The close link between the management of companies and the selling agency agreements into which companies enter has been a special feature of the working of the managing agency system in this country, and comments on these arrangements have been made by many critics of this system over the past decades. As long ago as 1936, when the then Companies Act was amended substantially to provide for safeguards against the mis-use of the powers of managing agents, section 87B of the Companies Act, 1913 as amended by the Act of 1936, required the consent of three quarters of the directors of a company before a managing agent or a firm of which he was a partner or any partner of such firm, or if the managing agent was a private company, any member or director of such company could enter into a contract for the sale, purchase or supply of goods and materials with the company.

7.28. The Companies Act, 1956, provided that no appointment of any sole selling agent would be valid unless it was approved by the company in general meeting within a period of six months from the date of the appointment. This restriction, however, applied only to sole selling agents and the powers of the directors to appoint other types of selling agents remained unaffected. The Companies (Amendment) Act of 1960 further tightened up the provisions relating to the appointment of sole selling agents. Under section 294 of the Act as amended in 1960, Government assumed powers to call for the terms of a sole selling agency agreement and to alter them, if as a result of this enquiry it disclosed that the terms were too enerous for the company to bear.

7.29. Several witnesses who appeared before us pointed to the inadequacy of the existing provisions of the law on the subject and pleaded for their tightening up. We have considered the problem in the light of a case study on the subject which was prepared by the Department of Company Affairs at our request. It appears that the type of cases under section 294 of the Act which now engage the attention of the Department fall under the following heads :—

(i) applications received from companies asking for the approval of Government to the appointment of their former managing agents as sole selling agents, within a period of three years from the date of their having ceased to act as managing agents of that company;

(ii) secondly, enquiries initiated on the basis of reports received from Regional Directors regarding the sole

selling arrangements of some companies. We were informed that instructions were issued to the Regional Directors in 1962 to submit reports to Government on such sole selling arrangements as were considered by them to be **prima facie** prejudicial to the interest of the shareholders.

7.30. The statistical position about applications under the above heads shows that only a very limited number of cases, falling under section 294, were considered by Government during the last few years. With the progressive abolition of the managing agency system, there is good reason to think that many of the erstwhile managing agents would like to enter directly or indirectly into sole selling agency agreements with the companies which they managed previously. Our attention has also been drawn to a growing tendency on the part of several companies managed by managing directors or managers exercising the powers of managing directors to appoint as sole selling agents the associates of such managing directors or managers, or the firms or companies in which such managing directors or managers are directly or indirectly interested. Section 294 of the Companies Act, as it stands at present, does not cover these cases. In the wake of the expected abolition of the managing agency system, it is important to take note of this lacuna in the present Act.

"We, therefore, suggest that Government should consider the strengthening of the provisions of section 294 of the Act, and particularly of sub-section 4(b) (ii) of this section so as to enable them to keep a close watch on the tendency to use the selling agency agreements as a device for unduly adding to the remuneration of the management of companies.

We were told that one reason for the difficulty which faces the Administration in dealing with this section arises from the uncertain interpretation of 'sole selling' and that taking advantage of this interpretational ambiguity, many sole selling agents try to evade the law by describing themselves as distributors, agents; sales promotion advisers sales brokers; etc. An additional complication is caused by the fact that the present section refers to sole selling agents 'for any area'.

The difficulty of defining selling agents and distributors so as to distinguish the former from the latter is considerable. Nevertheless, as the provisions of Sec. 294 are aimed only at selling agents and not distributors, we consider that it is very important that an attempt should be made to distinguished between these two categories. The distributors render an essential service in the marketing of goods. As long as their remuneration is commensurate with the services rendered by

them, there would *prima facie*; appear to be no need for regulating their appointments. Selling agencies generally and sole selling agencies in particular stand on a different footing inasmuch as they are usually remunerated on the basis of a commission on turn- over and it is not ordinarily easy to equate the value of their services with the commission payable to them. The present difficulty of distinguishing between selling agents and distributors has been, we were given to understand, a major impediment to the effective implementation of the provisions of this Section of the Companies Act. It is, therefore, necessary both in the interest of Administration as well as of the business community that an effort is made to distinguish these two categories as precisely as possible and in any case to give more detailed indications through executive instructions or otherwise to all concerned as to the types of cases conforming to prescribed standards which would not require approval by Government in individual cases and those which would need very special justification to obtain such approval from Government. In cases of deviations from the standard terms the prior approval of the Government should be obtained.

7.31 A more formidable difficulty arises from the lack of the requisite competence on the part of the present administrative personnel in the offices of the Department of Company Affairs to deal with knowledge and understanding with the provisions of this section. Even if the law could clearly define the cases where the approval of Government would be needed in future to the sole selling agreements entered into by a company, we doubt if the present staff of the Department would be able to deal adequately with them. We feel sure that the Department realises this handicap. It is, therefore, essential that if this section has to be properly administered, an adequate competent staff should be built up in different regions and they should be given very clear-cut guidelines as to what they should look for in these sole selling agency contracts which come up before them for examination. At present we do not think that any such guidelines are available to them.

A good deal of intensive home work will have to be done by the senior officers of the Department, in consultation with selected representatives of trade and industry and marketing experts, to evolve appropriate guide lines for the use of departmental officers entrusted with the responsibility for the administration of the provisions of the law relating to sole selling agents. The object of these guidelines would be (a) first, to work out the norms and yard sticks with reference to which selling agency agreements would have to be examined, and (b) to prescribe standard terms and conditions subject to which such agreements could be entered into.

7.32. We understand that several years ago, a detailed study on this subject was initiated in the old Department of Company Law Administration, but do not know if as a result of this or later studies any guide lines on this subject have since been evolved by the Department of Company Affairs.

If an effective administrative machinery could be built up for this purpose, but only subject to this condition, we would recommend that having regard to the importance of this matter, copies of all sole selling agency agreements entered into by public companies with a turn-over over a prescribed limit in any particular line of trade or industry should be submitted to Government for registration in the regional offices. It should be open to Government to modify the terms of these agreements at any time during their pendency after hearing the parties, concerned, and companies should be required to give effect to these modifications with effect from such date as Government might indicate.

As long as competition has no effective play in our economy, the marketing cost of industries should be a matter of concern to the public, since there is no assurance in such a situation, that the final costs of the goods and services to the consumers would not be unreasonably pushed up by excessive marketing costs.

7.33. There is one particular aspect of these costs to which our attention was drawn by a few witnesses. We were told that one likely bye-product of the proposed abolition of the managing agency system would be the appointment of relations and friends of managing directors or directors or of the firms and companies in which such directors were directly or indirecly interested as sole selling agents of the companies concerned. This development would need to be carefully watched.

We would recommend that if this tendency grows rapidly, the law should be suitably amended to require that in such cases the terms and conditions on which selling agency agreements were to be entered into should be approved by a special resolution of the companies concerned, within a period of six months from the date of commencement of these agreements, and that the commission or other payments proposed to be made to the selling agents in such cases should be suitably disclosed in the profit and loss accounts of companies.

7.34. A few competent witnesses brought to our notice some developments in company practice which appeared to be already under way in the wake of the anticipated abolition of

the managing agency system. They referred specifically to some new practices regarding the appointment of 'virtual substitutes' for managing agents in the form of Consultants, Technical Advisers, Agents or Special Officers, whom it was proposed to remunerate by commissions on profits irrespective of the value of the services rendered by them. We need hardly say that we attach a good deal of importance to the services of genuine Consultants or Technical Advisers, and realise the need for their services in many areas of industry in our country. From this point of view we would welcome the growth of such institutions.

It is, however, important to ensure that spurious organisations, calling themselves by these names, are not used as a device for channeling the profits of companies into the hands of the erstwhile managing agents or their associates. As a rule, we consider that the best way of remunerating genuine Consultants or Technical Advisers would be to compensate them by means of fees so calculated as to ensure that the payments are commensurate with the value of their services, and not by means of ad hoc percentages of commission on gross profits. Any how, these practices to which our attention has been drawn need to be closely watched by the Department of Company Affairs. In particular we suggest that where a percentage of gross profits is proposed as remuneration for such organisations, it should be subject to ratification by the company in general meeting within a period of not more than six months from the date of their appointment. Government in the appropriate Ministry may also consider a system of registration of Consultants, Technical Advisers, etc. who should be called upon to conform to certain essential minimum conditions before they are permitted to offer their services to the business community.

CHAPTER — VIII

Shareholders' Control and Minority Rights

The outlines of the scheme of legislative and administrative control over company management and company practice embodied in the Companies Act, 1956, stem from a view of the traditional concept of shareholders' control over company management, which is now being increasingly shared in most advanced countries of the world. In the early years of joint stock enterprise, the theory propounded by legal formalists stressed the primacy of shareholders' control. They were supposed to wield the levers of power in a company, and the so-called sovereignty of shareholders was almost a fundamental article of faith in the corporate jurisprudence of those days. The management of companies also delighted to describe themselves as the servants of shareholders, a habit which still lingers on in some antiquated management circles in this country.

8.2. The early reforms of Company Law were largely influenced by this formalist view of the role of shareholders in the affairs of a company. Several recommendations of the Expert Committee on Company Law reform, better known as Bhabha Committee, were based essentially on this view of the status and rights of shareholders, although in large parts it was qualified by a robust pragmatic recognition of the realities of shareholder control. In the result, many provisions of the Companies Act, 1956, provided for the first time that company decisions in many areas of company management and practice which had hitherto been left to the judgment of the Board of Directors should be subject to the approval of the company in general or special meeting. The underlying faith of company reformers at that time was that by placing these matters under the formal surveillance of shareholders, they were imposing a check on arbitrary decision-making and incidentally ensuring that these decisions were taken in the light of the views expressed by the shareholders. In its essence, this faith was perhaps not very dis-similar to the popular political argument, at that time, that the wider were the limits of popular franchise, the greater was the opportunity to the representatives of the people to take an intelligent and effective interest in the working of democratic governments.

8.3. Few informed people in any country of the modern industrial world where the corporate form is well developed

still retain any such faith in this view of the shareholders' democracy entertained by an earlier generation of corporate theorists. While it is now generally recognised that the shareholder has a vital role to play in corporate economy by insisting that an enterprise shall be profitable, by demanding full disclosure of the evidence provided by company accounts and other records of company performance, and by pressing their right to remove managements from office when they do not measure-up to their essential minimum duties and responsibilities or when businesses are run at continuing losses, the hopes of an earlier generation of company reformers that shareholders will continue to take an active part in directing the broad lines of a company's policies and programmes have largely disappeared.

8.4. Indeed in many knowledgeable circles a doubt has been expressed whether it is desirable that the shareholders should have any more effective role to play in the management of a company than they already do have under the existing provisions of Companies Acts in many countries including our own. Thus the Jenkins Committee in U.K. has observed that—

> **"It may be theoretically desirable that shareholders should have a more effective voice in the management of their companies' business ..... As against this, no company's affairs can be managed properly or indeed managed at all, otherwise than through a Board of Directors with a reasonably free hand to do what they think best in the interest of the company.*"**

It is true, in practice, that shareholders' control is ineffective partly because of their indifference and lack of adequate competent knowledge to guide the affairs of their company. It does not, however, follow that because of this their control over the business of a company should be removed or further diluted; nor does it follow that the need for giving the Board of Directors a reasonably free hand in management requires that such limited control as the shareholders now exercise over company affairs should be eliminated. As three distinguished members of the Jenkins Committee point out :—

> **"It is also said that shareholder control is inefficient, since directors, as a class, know better what is good for business than the shareholders themselves. In the normal case this in usually true. But if shareholder control is destroyed and nothing put in its place, we have to go still further and say that business efficiency is best ensured by allowing the directors to function free**

**Vide* page 3, para 14 of the Report of the Company Law Committee, 1962 (U.K.), Cmnd. 1749.

from any outside control, except that of the courts in the event of fraud or misfeasance and by making themselves irremovable, without their own consent, however inefficient they may prove to be@".

8.5 The practical problem stemming from modern developments in company practice which confront company reformers is how to reconcile reasonable control over the management of companies with the need for giving a reasonably free hand to them to do what is best in the interest of the company. Recent thinking in the advanced western countries of the world has been concerned with the problem of devising an appropriate internal forum, within a company's structure itself, where a reasonable balance of power between the management of a company, its shareholders and its employees can be struck. In the absence of any such institutional forum, our Indian they are thinking during the last decade has been concerned with the problem of providing external controls largely through machinery of the Administration.

We feel sure that it will be generally agreed that to the extent that an appropriate institutional structure is built up within the organisational frame of a company which provides a forum where the management of a company, its shareholders and its employees can participate in major decision-making, the need for external control over companies will correspondingly diminish. Till then, however, the working of companies and those responsible for their management need to be placed themselves under the discipline of a reasonable measure of statutory regulation and control. The aim of practical policy should, however, be to promote the growth of appropriate institutional structures within the constitution of a company, with a view to the progressive reduction in the area and rigours of external control.

It is against this background of what we consider to be right policy to follow in this field that we have considered some suggestions for further strengthening shareholders' control within the framework of our Company law.

8.6. Witnesses have suggested that if minority interests could be better represented on the board of companies, this in itself will provided some internal check on company management and company affairs. In this context the question of proportional representation of shareholders to the board of a company was

@Vide page 209, para 8 of the Jenkins Committee Report.

stressed by some witnesses. Section 265 of the Companies Act, 1956, permits a company, if it so chooses, to elect this method of representation on its Board by its shareholders. In practice, however, little use has been made of the powers already given to companies under this section. Several States in the U.S.A. have compulsory provisions for proportionate representation (by the method of 'cumulative voting') in the election of directors, and several other States in that country have permissive legislation for this purpose. Such recorded evidence as we have on the actual working of the system of 'cumulative voting' in the States of the U.S.A. where the State laws provide for compulsory proportional representation suggests that the obvious objections to this method are somewhat exaggerated.

Nevertheless, a great majority of Company managers in this country consider that it is better to have a cohesive Board, resulting from a straight majority vote rather than one containing conflicting groups or factions. Also the demand for proportional representation by the shareholders themselves or the shareholders' associations has been very limited. In these circumstances we do not consider that any amendment in the law is called for at present. We have already stated in para 6.10 (p. 64 . . . .) that the subject should be studied further.

8.7. Another suggestion which has been made before us is that if 10% of the shareholders of a company combine and ask for their representation on its Board, it should be obligatory on the part of the company to accede to this demand. Although, we appreciate the object underlying this proposal, we feel that if the minority shareholders could combine, they would not find it particularly difficult to elect one of their representatives to the Board, particularly in the case of companies where shareholding is disperesed.

We feel that much more concentrated thinking on the subject need to be done by the active minority shareholders and by shareholders' associations in different parts of the country, before they can legitimately seek the aid of legislation to support their moves.

8.8. It remains for us to consider what action that we can recommend to strengthen those provisions of the Companies Act, 1956, which enable shareholders to seek redress from Government or the courts of law in cases where companies are grossly mismanaged or are managed in a manner which is pre-judicial to their interest or oppressive to large sections of their shareholders.

8.9. Section 408 of the Companies Act was intended to enable the Central Government to take quick action to intervene in the affairs of a company if it was satisfied that the

affairs of the company were being conducted either in a manner which was oppressive to any members of the company or in a manner which was prejudicial to the interest of the company or to the public interest. This section empowered the Central Government to appoint not more than two directors who might or might not be members of the company as additional directors in such cases. It was expected that these nominees of the Central Government on the Board of the company would be able to pull their weight and to influence decision-making by the other members of the Board. In course of our evidence, we were told by witnesses that in the very few cases where these powers had been invoked by the Central Government, this expectation had been largely belied. The nominated directors were either ineffective or were overruled by the majority of the other directors on the Board. The section, as it stands at present, does not vest the Government directors with any special powers, and indeed does not arm them with such over-riding powers as they must necessarily have if they are expected to produce any impact on company management. Further, we were told that in some cases the appointment of Government directors was also challenged in courts of law.

Unless, therefore, this section in radically overhauled so as to empower the Government directors to intervene more effectively in decision-making by a majority in important matters, we do not think that it is likely to achieve the objects for which it was intended. We, therefore, suggest that Government should consider how this section could be suitably amended. One way of investing Government directors with effective powers would be to empower them to hold up decisions in respect of some specified areas of company management and to refer them to Government if they were of the view that such decisions would be oppressive to any members of the company or might prejudice the interest of company or might be against the public interest, if they were given effect to by the Board of the Company.

8.10. Sections 397 and 398 of the Companies Act empower minority shareholders to seek redress in courts of law in the circumstances indicated in these sections. We were told by witnesses that court action in such cases was usually dilatory and that according to the procedure followed by the courts it was not easy to expect expeditious disposal of the applications filed before them. In many cases, further, the courts were reported to be inclined to take a view of these provisions, which was largely coloured by the traditional thinking in legal circles on the internal management of companies as being primarily the responsibility of the majority of the Board of Directors. In a subsequent chapter of this report we have considered the desirability of suggesting an alternative machinery

for the adjudication of cases filed under these sections and all other sections which are now within the jurisdiction of the courts of law.

We would not, therefore, like to comment further on the defects and deficiencies in the administration of these sections, except to say that it seems to us that if the powers vested in the courts under these sections are to be effectively utilised, some far reaching changes in the structure of the judicial machinery as well as in the procedures and in the rules of business of the relevant judicial institutions would be essential. We shall revert to this theme in a later chapter.

There is, however, one important amendment to the existing provisions of these sections that we would suggest. At present the right to apply to a court of law under section 397 or section 398 of the Act can be exercised only by not less than one hundred members of a company or by not less than one/tenth of the total number of its members, whichever is less, or by any member or members holding not less than one/tenth of the issued share capital of the company, provided that the applicant or applicants has/have paid all calls and other sums due on their shares. The Central Government may, however, authorise any member or members of the company to apply to the court under these sections notwithstanding the above requirements. It was represented to us that since it took a good deal of time to obtain that authorisation from the Central Government in Delhi which had necessarily to ask for information from the Registrars located in out-lying areas before it could form its opinion whether it was just and equitable to authorise any one member or more members of a company to apply to a court of law under those sections, it would be desirable to do away with this requirement about the authorisation by the Central Government contained in sub-section (4) of section 399 of the Act.

Although a view was expressed in our Group that the removal of this requirement might lead to the abuse of the processes of law, we felt that if one or more individuals desired to apply to a court of law to have his or their grievances thrashed out, it would not be proper to deny them access to the courts and that if the courts fell that the processes of law were being abused it would be possible for them to take appropriate action when the applications were considered by them.

8.11. There is one point about the voting rights of shareholders on which we would like to comment. We have referred earlier to the apathy and indifference of shareholders and

their lack of competent knowledge to take an intelligent interest in the affairs of a company. Under modern conditions even the knowledgable shareholders of large companies who might be able to lead other shareholders are very often so dispersed geographically that it is impossible for them to get together and combine for effective action at company meetings. They have neither the time for nor the resources to undertake long journeys, nor can they afford to spend much time on the affairs of companies in which they are interested as shareholders. Under the law, as it stands at present, they may of course appoint local proxies but proxies have no right to speak at company meetings, although they have the right to vote.

We, therefore, recommend as already mentioned in para 6.11 (p. 65.). that the least that can be done to enable shareholders who are in a position to do so to express their views at company meetings is to confer on the proxies the right to speak at company meetings.

This is a much needed reform. We do not think that this privilege is likely to be abused. But even if it were to be abused in a few cases, we do not see that there is any other convenient way of enabling shareholders, under modern conditions, to express views on matters of direct interest to them. We may note that even the very conservative Jenkins Committee in the United Kingdom recommended this amendment in the law of that country. If this facility needed to be provided to shareholders in a geographically small and compact country, the need for a similar provision in a country of continental dimensions, like ours, hardly requires any emphasis.

8.12. An important aid to shareholders' control over company management is provided by the provisions of Company Law relating to the preparation and presentation of company accounts and their audit by professional auditors. The progressive elaboration of the requirements of the law relating to the audit of company accounts is not only an indication of the growing complexity of business methods and practices but also a recognition of the increasing importance of protecting shareholders against such involved financial manipulations as can be unravelled and meaningfully disclosed to the shareholders only by professionally trained experts. Company Auditors have, however, to be not only professionally competent but must also possess integrity and independence of the character if they are to discharge their duties to the shareholders honestly. A point was made to us by several witnesses that although it is the prerogative of shareholders to appoint the auditors, in fact they are mostly the nominees of the management, and whatever the law could do to strengthen the position of latter *vis-a-vis* the management would help to

increase their independence. We see no easy way of doing this. This is a responsibility of the accounting profession and we must continue to rely on the quality of leadership which the profession can throw out. Negatively, however, the law has already provided certain safeguards regarding the appointment and reappointment of Auditors and the Chartered Accountants' Act also contains some provisions intended to strengthen the profession. There is, however, one suggestion which we would like Government to consider. It was proposed to us by some witnesses that, human nature being what it was, it was undesirable for even professional people to continue to be attached to particular companies for more than a limited period, say, not exceeding five years.

We have given some thought to this suggestion and feel that there may be some advantages in changing the Auditors of companies at least every five years.

This would give the shareholders of a company an opportunity of obtaining the advice and assistance of different firms of Auditors, periodically, instead of having to rely on any one firm indefinitely.

We recommend that this proposal should be examined by Government in consultation with the Institute of Chartered Accountants before any change in the existing law is made.

8.13. In recent years the type of audit to which most company accounts are subject has been the subject of much intensive debate. The views of enlightened shareholders and theorists of company finance on the one hand, and the practitioners of profession of accountancy on the other continue to diverge on the type of audit increasingly required in the circumstances in which the business is carried on at present and is likely to be conducted in the future. 'Efficiency audits' and 'social audits' have been suggested alike by representatives of shareholders and professional students of business finance, as being increasingly necessary to supplement the type of traditional audit now conducted by company auditors. We are aware of a few progressive business houses of the country which have recently taken some steps to instal system of 'efficiency audit' which seek to measure the factors underlying a company's ability to contribute to national income and growth rather than only to its profits. But the reports of such audits are rarely disclosed to the shareholders or the public. 'Social audits' still continue to remain a rare exercise in this country. Their object would be to try and deal with the relations of an enterprise with the various interests which focus on it, e.g., the consumers, the local community and the general public. In many other modern countries audit techniques and procedures based

on well-established rules of good practice in fields as diversified as industrial relations, or the relations of a company with its suppliers, distributors, or government departments have been devised. We are not sure if the accountancy profession in this country has so far given any thought to the study and analysis of the accounting problems involved in the measurements of these relations. But 'efficiency' and 'social' auditing require specially trained company auditors of the requisite calibre. In our country we have a few competent firms of industrial consultants, but although 'efficiency' auditing has tended to develop out of industrial consultancy, the two things are not quite the same. Consultants are now increasingly called to advise promoters and company management on particular aspects of a firm's performance, but 'efficiency' audit is concerned with its *overall* performance. 'Social' auditing is still more complicated in that it requires an analysis of values and attitudes as well as of organisation and techniques. We do not know if the accountancy profession in this country whether through the Institute of Chartered Accountants or the Institute of Cost & Works Accountants has undertaken any special studies on the principles of 'efficiency' or 'social' auditing or if the present course of studies prescribed for students of accountancy, whether at the junior or the senior level, provide for their adequate training in the principles of this special form of auditing.

Be that as it may, a good deal of detailed study will have to be undertaken into the principles and contents of both 'efficiency and social audit' before appropriate procedures and techniques in respect of such audits can be evolved. Till then it is hardly possible for any Companies Act to require that the accounts of public companies or, at any rate, of some of them, should be subject to such audits. We do not, therefore, consider it practicable at this stage of the development of the accounting profession in this country to provide compulsorily for such audits in our Companies Act in respect of public companies whether in the private or public sector.

8.14. We refrain from expressing any views on the audit of Government companies as this subject has been discussed in the report of the Study Team on Public Sector Undertakings and the Administrative Reforms Commission has already considered its recommendations. In the light of what we have already stated in the previous paragraph about the need for much more intensive study and research on the principles of 'efficiency' and 'social' auditing in this country, it is necessary for us to emphasise that the problems involved in the installation of any system of 'efficiency' audit and, to a much greater

extent, of 'social audit' are not so much organisational or administrative as essentially, technical. Neither among the company auditors dealing with the accounts of companies in the private sector nor among the official auditors beloging to the offices of the Comptroller and Auditor-General or the Director of Commercial Audit do we have at present many persons who have either sufficient acquaintance with the principles of such audit or who are familiar with the methods and techniques which have to be used in these types of audit.

Till the profession of accountancy in this country has built up a cadre of such highly specialised auditors, it would be futile to emulate the example of other countries and try to duplicate institutions which have been set up elsewhere.

8.15. This deficiency in the equipment of our technical personnel, however, needs to be made good without delay.

We, therefore, strongly urge that Government should do all that they can to help the Institute of Chartered Accountants and the sister Institute of Cost & Works Accountants to develope technical and research sides. They should be encouraged to undertake high grade study and research into the principles of 'efficiency' and 'social' auditing, and into the methods and techniques appropriate to such special audits. Simultaneously, the Institutes should be suitably assisted so that they can secure access to the best available knowledge on this subject in some of the Western countries; and, through a system of exchange of personnel may be able to build up a cadre of well trained specialists within its ranks. It is only then that thoughts about 'efficiency' and 'social' audit can become a reality in company audit in this country instead of remaining, as they now mostly seem to do, merely heavy loaded phrases which only embody vaguely articulated hopes and intentions.

We sincerely trust that nothing that we have said in the foregoing paragraph implies any criticism of the work that has so far been done by the Institute of Chartered Accountants or the Institute of Cost & Works Accountants. But if the accountants of today are to equip themselves adequately for the tasks and responsibilities that await them in the future, it is essential that a great deal more will have to be done both for the education and training of young recruits to this profession and for developing specialised knowledge and competence in those areas of accounting and audit where the profession must take increasing account of the new economic and social problems created by the emergence of the modern corporation, whether in the private or the public sector.

CHAPTER IX

Inspection, Investigation and Prosecution of Company Cases

One of the terms of reference of the Working Group calls for the examination of the adequacy of the administrative machinery for preventing malpractices in company management. This has been the traditional function of Registrars of joint stock companies both in England and in this country. The basic framework of the law applicable to this subject was provided by sections 234 to 255, as they stood in the Companies Act, 1956. These sections were modelled on sections 164 to 175 of the English Companies Act, 1948 with some minor changes here and there. The first Companies Act Amendment Committee appointed in 1957, within less than a year of the coming into force of the Act of 1956, under the chairmanship of late Shri A. V. Viswanath Sastri, a former judge of the High Court of Madras, commented on the adequacy of these provisions as follows :

> **"Though steps have been taken under them against a few companies, they have proved mostly infructuous. Representatives of shareholders as well as the Department stressed the need for tightening up of these provisions, while those representing the management consider them to be unduly inquisitorial and harmful. Very little has been achieved in the way of reformation or redress by setting in motion these provisions. They require amendment if they are not to remain a dead letter."**

One of the earliest Annual Reports on the Working and Administration of the Companies Act, 1956 submitted to Parliament described the then powers, in the 1956 Act as providing the Administration with a 'big jaw' with only a few teeth in it.

9.2. In order to understand these comments fully, it is necessary to trace very briefly the evolution of the law on this subject.

9.3. The Companies Act, 1956 (Act I of 1956) did not empower the Registrars of Companies to inspect the books of account of a company required to be kept under section 209 of the said Act. In the light of their experience in administering the Act, the Registrars found that they were handicapped in the discharge of their duties. As long ago as 1957, it was pointed out to the Companies Act Amendment Committee by the then Department of Company Law Administration, that as in the

case of Directors, the Registrars should also be given the right to inspect the books of a company whenever they thought this to be necessary. But the majority of this Committee were of opinion that the grant of this power was not called for, in view of the proposed amendment to section 234 giving powers to the Registrar to call for the books of account of a company. At a later date, however, when the Companies (Amendment) Act of 1960 (Act 65 of 1960) was enacted, the following proviso to sub-section (4) of section 209 was incorporated in the Act—

> **"Provided that the books of accounts shall also be open to inspection by the Registrar or by any officer of Government authorised by the Central Government in this behalf if, in the opinion of the Registrar or such officer, sufficient cause exists for the inspection of the books of account."**

9.4. This new Proviso to section 209(4) of Companies Act for the first time empowered a Registrar or any other officer of Government authorised by the Central Government to inspect the books of account of a company as a matter of their normal administrative practice, but the exercise of this power was conditional on the Registrar or the authorized officer duly satisfying himself in the first instance that there was 'sufficient cause' for an inspection. 'Sufficient cause' for the purposes of action under section 209(4) was not defined anywhere, but the words were taken to mean a situation in which the Central Government or the Registrar reasonably considered that correct information about one or more major aspects of the working of a company could not be obtained at all or within any reasonable period of time, except through an inspection of its books of account, or that there was likelihood of these books being destroyed, or that the allegation about the books of account not being properly kept was *prima facie* made out. This power could also be exercised justifiably if there was a reasonable fear that the books of account might be destroyed. The aim of the proposed inspection was, in short, to elicit information on specific points or to ensure that the information already supplied was correct. Under this provision the inspection of the books of account of companies is undertaken by Registrars.

9.5. We were informed that their enquiry usually covered the following types of scrutiny :

(i) Procedural scrutiny ;

(ii) Technical scrutiny ;

(iii) Special/Intensive scrutiny ;

(iv) Enquiries on complaints from shareholders and others; and

(v) Enquiries under section 234(1) or (7) initiated for reporting under section 234(6) for investigation into the affairs of companies under section 235 or taking action under section 233A.

9.6. The powers of inspection of the books of accounts under section 209(4) of the Act were reviewed in 1964 after the Joint Committee which considered the Companies (Second Amendment) Bill, 1964 had expressed the view that inspections undertaken by the Registrar or any other officer authorised by the Central Government (Company Law Board) should be a regular routine feature of administration and not merely of an *ad hoc* or special nature. The amendments to section 209(4) of the Act introduced by the Companies (Amendment) Act, 1965 provide *inter alia* that "The books of account and other papers shall be open to inspection during business hours (i) by the Registrar, (ii) by any officer of Government authorised by the Central Government in this behalf—provided that such inspection may be made without any previous notice to the company or any officer thereof." (*vide* section 209(4)(b) of the Act).

9.7. According to the clarifications issued by the Department we were told that enquiries under the amended sub-section (4) of section 209 were intended to cover following categories of cases :—

(a) Intensive Inspection for specific purposes on receipt of complaints, or when some serious irregularity was suspected or for the scrutiny of any documents on receipt of any specific information.

(b) Regular Inspection.

9.8. A departmental Committee appears to have examined the whole question of inspection under the amended section 209 of the Companies Act. On the basis of the report of this Committee, a Central Inspectorate under a Director of Inspection with special agencies operating in the regions, for undertaking 'routine inspections' under the guidance of a Director of Inspection and Investigation was established at the headquarters of the Department of Company Affairs at New Delhi. The guiding principles of the inspection directorate were enunciated in the note dated 5th November, 1965 recorded by the first Director of Inspection and Investigation. It is stated in that note that "the object of inspection is to evaluate precisely the *level of efficiency* attained by an organisation. An Inspector under section 209(4) should, however, be able to report whether conditions do exist or have been created which would enable the organisation to function efficiently. Its role

is much wider than that of 'statutory audit' on behalf of the shareholders of the company. While statutory auditors have naturally to go into the details of every transaction to satisfy themselves that the transactions have been validly entered into, in accordance with the rules and procedures of the company, the object of inspection would be not only to see to what extent the auditors have done their duties but also to take a broader point of view and examine the rules and procedures themselves. In this respect inspection must transcend the comparatively narrow limits of audit. It may satisfy the auditors if commitments have been made and expenditure has been incurred in accordance with the accepted procedure of the company. The Inspector must, however, ask himself and report whether these procedures themselves are sound and whether the transactions in question have been in the best interest of the company. The actual inspection of the books of account will, therefore, greatly depend upon the evaluation of the internal control and management set up of the company."

9.9 A careful consideration of the legislative history relating to the inspection of companies and the impressions which we received from such evidence as was placed before us at Bombay, Madras and Calcutta, however fills us with doubt if the amended section 209(4) of the Act was intended for the purpose mentioned above. Our misgivings are accentuated by the fact that we do not see that in the near future the Department or any other organization would acquire the high degree of technical competence essential for undertaking the type of 'efficiency' or 'propriety' audit, which might have been the intention of the Department to undertake in the beginning as a regular 'routine feature' of administration. As we read the legislative history of the progressive amendment of section 209(4) of the Act between 1956 and 1965, we are inclined to think that the first amendment of 1960 and the latest amendment of 1965 were intended primarily to facilitate the normal work of the Registrars of Joint Stock Companies and in particular to find out whether the materials and facts in relation to particular companies would justify initiation of action under section 234, 235, 237 or 249 of the Act. This seems to us to have been the real intention of the legislature underlying the amendment of section 209(4) in 1965, when it decided to do away with the requirement about 'sufficient cause' and the need for giving previous notice to the company or any of its officers.

In this view we consider that the original objective underlying the present procedure as well as the organisational set up for implementing the provisions of section 209(4)(b) of the Act for evaluating the level of efficiency of companies was not very realistic, however laudable in theory it might have been. It can, however, be a useful instrument for finding out materials

and facts which could justify initiation of investigations, inspections and 'special audits'.

9.10. The officers and staff allocated to the Directorate of Inspection are under the functional control of a Central Director of Inspection although they work in the regional offices. The Working Group was told that the inspection staff were not under the direct and effective administrative control of the Regional Directors, who were, therefore, inclined to take little interest in their work and did not feel that they had that measure of direct responsibility for this aspect of Department's work as for other work of the Department in the region. We are aware of the recent effort in the Department to ensure better co-ordination of work between the Central Directorate of Inspection and the regional offices.

At the same time it was brought to our notice that there might be and in fact there was some conflict between the regional offices and the Directorate of Inspection in relation to inspection work. Such conflict of functions was likely to impede cohesive and harmonious working in this field.

We feel that it is essential to integrate the work of inspection officers at the regional levels, with the field organisation of the Regional Directors and Registrars. This would mean in practice that the officers attached to the Inspection Wing in the regional offices should work wholly under the administrative control of Regional Directors and should form part of the set up of regional offices. This will fasilitate their working in close concert with the Registrars of joint stock companies who are already under the control and supervision of the Regional Directors. The Director of Inspection and his staff at the headquarters of Department at Delhi should be concerned primarily with the formulation of principles of inspection and its methods and techniques and provide technical guidance, where needed, to the Regional Directors and the regional inspection staff. There will still remain a good deal of detailed home work to be done at the headquarters of the Department in evolving appropriate principles of inspection for the guidance of the departmental staff and for working out an integrated procedure relating to the implementation of sections 209(4), 234(6), 235, 237, and also section 233A of the Act dealing with the special audit of companies. The powers conferred on the Administration under these various sections are at present exercised on a somewhat *ad hoc* and haphazard basis, and no unifying principles or integrated procedure for appropriate action under these different sections appear to have been so far evolved. This

is a task for which we suggest the Director of Inspection at the headquarters of the Administration with the nucleus of staff stationed there should concentrate. Our proposals for the reorganisation of the work of inspection are, therefore, as follows :—

(1) The Central Directors of Inspection should be concerned with the formulation of the principles of inspection and the methods and procedure to be followed by the inspecting officers and their staff after periodical consultations with the Regional Directors;

(2) he should also be entrusted with the duty of working out similar principles and procedures for initiating action under sections 234(4) and section 233(A) of the Act relating to the special audit of companies;

(3) he should further offer, whenever necessary, technical guidance in individual cases to the Regional Directors and the regional inspection staff, and in all cases of inter-regional inspection where a carefully concerted strategy of inspection will have to be devised for the officers and staff of different regions, to ensure effective co-ordination of work among them;

(4) the administrative responsibility for the day-to-day supervision and control over the work of the inspecting staff should vest in the Regional Directors;

(5) the reports of the inspecting staff should be finalised in consultation with the Regional Directors, and in cases of inter-regional inspections, after consultation with the Central Director of Inspection; and

(6) on the basis of inspection reports the Regional Directors should take such follow-up action as may be needed in all matters in respect of which powers have been delegated to them under the Act.

9.11 The reorganisation of the work relating to the inspection of books of accounts of companies that we propose will, we hope, also incidentally help to strengthen the existing "special/intensive scrutiny cells" as they are called in the offices of the Registrars of joint stock companies. Reference was made in an earlier paragraph in this chapter to the types of routine scrutiny of annual accounts and other periodical returns that are submitted to the Registrars of companies. This work is now mostly entrusted to clerical staff with such help as so-called 'technical' assistants (generally junior commerce graduates) can give them. We are not sure that much useful purpose is served by the type of over-routinized and largely mechanical work that the present staff in the 'scrutiny cells' in the offices of Registrars of companies are now required to do.

We suggest that the work and organisation of these 'cells' should be reviewed at a very early date, and steps should be taken to cut out all infructuous exercises and to concentrate on selective meaningful scrutiny of annual accounts and other routine company returns that are now submitted to the Registrars of companies. At the same time advantage should be taken of our proposals for the re-organisation of the work of inspection to strengthen the 'scrutiny cells' in the offices of Registrars of companies with personnel of a higher calibre and quality. This may be done by replacement of some of the existing clerical staff by qualified technical people.

9.12. The statutory annual reports of the Department of Company Affairs give details of various investigations and special audits ordered by Government under the appropriate sections, i.e., 237(b), 249 and 235(c) of the Companies Act.

9.13. As a rule, it is only after the Department is satisfied after a preliminary enquiry that there is adequate material for such investigation or special audit that such a step is taken. In its Fifth Annual Report on the Working and Administration of the Companies Act for the year ending 31st March, 1961, the Department had set out the principles on the basis of which the decision to order an investigation into the affairs of a company is taken. We need not repeat the observations contained in that Report.

We would, however, suggest that in future inspections under section 209 should ordinarily be the first preliminary step to an investigation under Section 235 or 237 of the Act.

As we have already stated, the latest amendments to section 209 of the Companies Act were intended primarily to facilitate further detailed enquiries under the Act whether by way of investigation or special audit.

9.14. With regard to the special audit of companies under section 233A, we regret to observe that this power has been hardly used by the Administration although this section was incorporated in the Companies Act as early as 1960.

We understood that this was due to the fact that in a few cases the Administration was threatened with 'writ applications' in the High Courts against any move under this section of the Act to order special audit of companies. This may have been

the main reason for the relative infructuousness of this section but we are also inclined to feel that the absence of detailed principles and procedures, on the basis of which alone appropriate action under this section could have been initiated by the Administration might have also been major contributory factor.

9.15. In order to ensure more effective action under the aforesaid sections of the Act,

We consider it essential to create a combined office of Director of Inspection, Investigation and Prosecution at the centre.

We have already recommended that the Director of Inspection should be relieved of a good deal of his executive and administrative functions which properly belong to the regional field offices and should be concerned, so far as inspection is concerned, primarily with the formulation of principles and procedures and the tendering of technical advice, specially in cases of inter-regional inspections. This should enable him to take over the much more important task of directing investigations and later on of following up the results of such investigations with the help of competent and adequately trained technically qualified officers.

For this purpose the proposed office of the Central Director of Inspection. Investigation and Prosecution should be manned with persons possessing expert legal and accounting knowledge, training and experience.

All cases of inter-regional importance should be under the supervision of this office with such help and support the staff of this office might need from the regional and the state staff.

9.16. This Office should have broadly three divisions, (a) one, dealing with policy matters, i.e., the formulation of principles and procedures, including methods and techniques, for inspection, investigation and prosecution of compaany cases; (b) an executive division dealing with inter-regional or all-India investigations and (c) a second executive division dealing with prosecutions arising out of such investigations.

9.17. Advantage should be taken of the proposed re-organisation of the present Directorate of Inspection in the manner indicated above to bring into this Directorate those secretariat branches which are at present concerned with inspection, investigation and prosecution, so that unnecessary duplication of work between the

Directorate and the secretariat branches may be avoided. We have not had the time to work out the details of the set up at the headquarters of the Department of Company Affairs which will be needed for this purpose. This will be doubt be examined by the Department of Company Affairs in due course, but we suggest that it may facilitate decision making and the implementation of decisions, if the senior officers of the Directorate as proposed to be reorganised are given appropriate secretariat status.

9.18 We hasten to add that our recommendations as to the organisation and functions of this new office does not imply that the Regional Directors or the Registrars would be relieved of their work relating to the investigation and prosecution of relatively small cases of local importance. They will continue to be responsible for the handling of such cases, but here, as in the case of inspections, they will be entitled to call upon the technical help and guidance of the new office in all important cases or even in regard to other cases where they feel that such help is needed by them.

9.19 Section 388B confers on the Central Government the power to refer cases against managerial personnel to a court of law. If our recommendation relating to the formation of a Companies Tribunal is accepted, we suggest that all such case should be referred to that Tribunal. Although this section was hurriedly inserted in the Companies Act at the end of 1963, we understand that very little use has so far been made of it. Here again this is probably attributable to the fact that the Administration has not worked out the detailed principles and procedures that should be followed before any action was initiated under this section. In the absence of such detailed study it was naturally difficult for the Department to start any proceedings under this section. Further, in the only case in which the powers under this section were invoked by Government, the procedure adopted by the then Companies Tribunal was so needlessly involved and time-consuming that even after the lapse of three years little progress with the proceedings initiated by Government was recorded. It is clear to us that in order that effective use can be made of this section, it is necessary for the Administration to formulate clear cut objectives and policies on this matter, to see that a summary procedure has been evolved for dealing with such cases, and that a properly constituted Tribunal manned by qualified and experienced persons with adequate knowledge and understanding of company methods and practices who are in a position to pronounce with authority on issues of business ethics and morality has been set up.

9.20 Section 635B of the Companies Act limits the powers of a company to discharge, or to punish otherwise, an employee,

during an investigation under sections 235, 237, 239, 247, 248 and 249, or during the proceedings against managerial persons under section 388B. It is not necessary that in all cases of mismanagement, recourse should be had to section 388B. The alternative remedies under sections 397 and 398 could be resorted to whenever any issue of public interest is involved. It has been claimed that *prime-facie* the protection sought to be given to the employees under section 635B of the Act should be available also while proceedings under sections 397 and 398 are pending. In support of this claim, it has been argued that the reason for which references to sections 397 and 398 were omitted in the Ordinance on this subject which was afterwards replaced by section 635 of the Act was that the time when the Ordinance was promulgated, the question of filing a petition under section 397/398 of the Act in the particular case which gave rise to the Ordinance was not even discussed, and subsequently this application became necessary in view of certain developments that took place after the petition under section 388B was filed before the Tribunal. We were inclined to accept the logic underlying this view.

9.21 Apart from the necessity for amending section 635B of the Act to cover cases of employees who might be called to give evidence in petitions under sections 397 and 398 it has been represented to us that there is considerable justification for extending this protection to these employees after the proceedings under all these sections have been concluded. It has been contended that even if the evidence of employees is tested and found correct but a complete change of management is not possible, (relief could often be by way of adequate minority representation and cannot in all cases deny representation for the majority) the said employees would be exposed to the risk of punishment by the new management at the end of these proceedings, and there is, therefore, adequate justification for amending the section so as to provide for such protection as is now available, on a permanent basis, that is, till the expiry of the normal period of retirement of the employees according to the rules of the company concerned. We have given some thought to this difficult question.

In our view such cases call for an appropriate balancing of the equities involved with the basic needs of sound management practice. In this view we find it difficult to accept the plea for permanent protection. Instead, we suggest that in such cases, the period of protection given under section 635 of the Act should be limited to a period of five years from the date of conclusion of the proceedings before a Court of Law of Tribunal or submission of the report by the Inspector, whichever may be later. We agree that this limitation on a

company's power to punish its employees cannot be construed as an unreasonable restriction as it merely subjects the company's action to a review by the Central Government. Further, it will be open to judicial authority, i.e., the appropriate High Court or a Tribunal to review Government's objection on an appeal to it. This will, we hope, ensure that the interests of management are not unduly affected.

ADDENDUM TO CHAPTER IX

(A note submitted to Chairman by Shri S. Venkataraman, Member Secretary, Working Group on Company Law Administration).

The provisions of Section 209 (4) relating to inspections are very useful to the Registrar of Companies in carrying out his statutory duties. But there is a danger in allowing it to be done in a haphazard maner. These inspections will have to be done under a regular chalked out plan duly approved by the Company Law Board. It will also be necessary to augument the technical staff at the regional and state headquarters.

These provisions would also enable the Central Government, through the authorised officers, to look into the cases where serious complaints have been received. The Inspection provisions of section 209 are not a substitute to the investigation provisions of sections 235 and 237 or the special audit provisions of section 233-A. But the inspection under section 209 would enable the Government to check up the various complaints and also to look into the way in which the business is being conducted. Further, it may be necessary to have studies of working of Group companies and companies industry-wise, spread out in different places. The results of the inspections may enable the Central Government to decide further course of action, including amendment of the Act. For this purpose it is necessary for the Central Government to have certain inspections carried out through the Director of Investigation and Inspection. There should, therefore, be small independent Wings at important centres to conduct such inspections under the functional jurisdiction of Director of Investigation and Inspection. This can be compared to the Inspection Directorates of the Income-tax Department and the Central Excise and Customs Department, etc. At present, there is only a limited staff and they attend to important cases of complaints and group companies and they have necessarily to be under the functional jurisdiction of the Director of Investigation and Inspection.

CHAPTER—X

Discretionary Powers under the Companies Act.

One of our terms of reference specifically requires us to examine if any clearly defined criteria have been presented under rules or administrative instructions for the exercise of the extensive administrative discretion vested in the Central Government under the Companies Act. It will have been seen from what we have said in chapters VII and VIII of this report that under the scheme of regulation envisaged in the Companies Act, 1956, a large amount of discretionary authority has been vested in the Administration. That this was done as a matter of deliberate policy is clear from the debates in Parliament and the record of the discussion in the Joint Select Committee of Parliament on the Companies Bill, 1953. We would only quote a few lines from the statement made by the then Finance Minister, who was in charge of the Bill. Speaking in the Lok Sabha on a Motion for the reference of the Bill to the Joint Committee of both Houses of Parliament, he observed "..... Hon'ble Members will expect me to say a few words about our plans for the adminstration of the Companies Act in future. Lord Cohen, Chairman of the Company Law Reforms Committee, 1943—45 of the United Kingdom, ... himself a great authority on commercial and mercantile law in that country, once observed that no modern system of Company Law could be satisfactorily administered except through a strong and competent civil service, for it was of the essence of any such system that effective powers must be given to the Executive and a large measure of discretionary authority must, of necessity, be vested in the organisation responsible for the adminstration of the Companies Act. I share these views, and am, therefore, fully seized of the importance of building up a competent administrative organisation ....."* Speaking in a similar vein, the Company Law Committee of 1952, popularly known as the Bhabha Committe, had earlier observed that "in so far as changes in the Law are concerned, our proposals attempt to secure the fullest measure of disclosure of information relating to the activities of companies and the imposition of such restrictions on these activities as we have considered necessary in the present state of company practice in this country. Some of these restrictions would no doubt appear irksome to business which is conducted in the efficient and honest manner, but reforms in all fields of group activity must necessarily be based on average behaviour. It is part of the social discipline of our times that institutions, no less than individuals,

*Lok Sabha 28th April, 1954,—*vide* Debate IV, No. 55, Column 5968.

which are in advance of the average standard have to submit themselves as much to the rigours of the law as these that are below that standard. Nevertheless, we have taken all possible care to see that our recommendations do not impose any unreasonable burden on legitimate business ..... and it is essential that there should be some flexibility in the Company Law ....."*.

10.2. It is against this fundamental problem of balancing the need for flexibility in individual cases in the context of severe rertrictions imposed on the company management and company practice based on the experience of average company behaviour in this country that the exercise of the discretionary powers vested in the Administration has to be considered. The growing complexity of modern life and the minimum postulates of social justice which are now part of the established public philosophy in all civilised countries has necessarily resulted in a vast expansion of governmental functions and vest in the Executive branches of governments in all countries with enormous discretionary powers. The problems of practical policy are broadly two-fold positively how to ensure that these powers are exercised in the public interest; and negatively how to safeguard the business of individuals and private bodies against the arbitrary use of these powers. We are not concerned in the Working Group with the political and constitutional problems of checks on the exercise of such powers and, therefore, confine ourselves only to the administrative steps which we consider necessary to ensure that these powers are used objectively, faily and impartially

10.3. The most important of these adminstrative safeguards is the formulation of detailed guidelines for the use of the different types of discretionary powers by the Administration, at all its hirarchical levels, within the broad frame of the provisions of the Companies Act. The importance of this step was emphasised again and again in course of the debates in Parliament in 1954-55 on the Companies Bill, 1953. In pursuance of the assurance then given by the representatives of Government suitable procedural rules and detailed instructions for the guidance of the departmental officers on the one hand and the members of the business community on the other were laid down. Elaborate forms were also prescribed with the object of assembling the essential data on the basis of which administrative decisions in these cases were to be taken in a convenient summary form. The earlier Annual Reports on the Working and Administration of Companies Act, which, by law, have to be placed before Parliament every year, contained summaries of the principles and procedure laid down by Government for the exercise of their discretionary powers in different areas of the Companies Act, 1956. By their very nature, however, these principles cannot be always

Vide Page 220 of the Report of the Company Law Committee, 1952.

reduced to mathematical formulae. Decisions on individual cases have, therefore, still to depend a great deal on the understanding and judgment of the officers exercising the discretionary powers.

10.4. We consider that there are two major directions in which the present position about the use of discretionary powers under the Companies Act can be appreciably improved.

We feel that there is still need for a good deal of more intensive home work in the Department of Company Affairs on the guiding principles relating to some of the discretionary powers vested in the Administration.

We have already refered to this ned in Chapter VII of our report.

Secondly, we consider that these guiding principles should be disseminated among the members of the business community as widely as possible.

Many of the businessmen do not read through Annual Reports of the Department of Company Affairs. Even in Parliament it is not often that these Reports are fully discussed. In the result, the guiding principles which the Department may have laid down and the rules and regulations which they may have prescribed, to facilitate the consideration of cases falling within the discretionary authority of the Department; very often go unnoticed, and a feeling is created among those who are affected by the exercise of these powers that they do not know where they stand in their dealings with the Administration.

We, therefore, suggest that the following steps may be taken in regard to these guiding principles:

(i) **the representatives of the interests likely to be affected by the use of disoretionary powers should be informally consulted before the guiding principles are finally drawn up by the Department;**

(ii) **these principles should thereupon be brought to the notice of all recognised Chambers of Commerce and Trade Associations including the Trade Unions and Consumers Associations where they exist;**

(iii) **adequate publicity through the departmental publications, the Press and by other means should be given to these guiding principles;**

(iv) **the Regional Directors and Registrars of Companies in the different states should expalin these guiding principles at formal or informal meetings to all**

those who may be affected by them in the leading centres of trade and industry within their jurisdiction.

10.5. We consider it very important that the Annual Reports submitted to the Parliament from year to year should be debated fully within the limits of time available for this purpose having regard to the exigencies of Parliamentary business. Parliamentary vigilance in such matters should be reasonably effective and not merely symbolic. Likewise, the chambers of commerce and trade associations should also make a special point to study, examine and consider the guiding principles which the Administration may have laid down from time time instead of merely confinding of themeselves to generalities of economic phhilosophy or economic policy. For this purpose they would need to organise their work properly, and must be served by personnel of the requisite education, training and competence.

10.6. The Companies Act, 1956 provided an important institutional safeguard against arbitrary or discriminatory exercise of the discretionary powers vested in the Administration. This was the function of the statutory Advisory Commisison established under section 410 of the Companies Act, 1956 as it stood in that Act. This permanent Advisory Commission was entrusted with the duty of advising the Administration on all those matters involving the eexrcise of discretionary powers which were specifically enumerated in the then existing section 411 of the Companies Act, 1956. Under the terms of this old section, it was further open to Government to refer to the Advisory Commission any other matter on which it might like to have its advice.

10.7. As we have already stated, the major dilemma of reconciling the requirements of general policy with the need fo flexibility in dealing with individual cases, on their merits. exercised the minds of the legislators a greal deal when Parliament was considering the Companies Bill, 1953. Fears were then expressed that if the powers to pass judgment on individual cases were left exclusively to the Administration, decisions might be taken not always on objective grounds in conformity with general guiding principles which Government might lay down, but to suit the personal likes and prejudices of individual officers or Ministers. A strong body of opinion both in the Committee of Parliament and in Parliament itself, therefore emphasised the desirability of setting up a statutory authority outside the administrative machinery of Government for the administration of the Companies Act. This had also been the recommendation of the Expert Committee on the amendment of Company Law, popularly known as the Bhabha Committee. As against this view, the official view was that the administration of the Companies Act—particularly those provisions of it which

dealt with the problems of management—went to the heart of the economic policy of Government in its application to the corporate sector, and could not be left for decision to any outside statutory authority. We quote the following statement made by the then Finance Minister which throws some light on the considerations that weighed with Government at that time in deciding against the establishment of a statutory administrative authority. "I cannot imagine how Hon'ble Members are suggesting that there should be a Commission with powers which are completely independent of the Minister. It will then mean that, indirectly, they want a Commission which will be independent of themselves, that is to say, the Parliament .... These matters are not juridical, they are not capable of that kind of fine precision. For instance, the word 'usually' is used in connection with many of the clauses in the Bill; so are the words 'public interest' or 'national interest'. I say that it is for (a) Parliament and (b) for the Ministers, who are responsible to Parliament to decide from time to time what is the national interest and what is the public interest. This is all the more necessary in these days, when one's prevailing philosophies are undergoing a change under the stress of developments in this country and elsewhere. In other words, we are living in a fast moving age and it is impossible to crystallise all these thoughts and to hand them over to a commission of experts who have learnt their expertise in different fields ..... Therefore, there should be the ultimate power left to Government to intervene, trying to interpret the wishes of Parliament in those matters of economic policy or industrial policy ....."*

In the event, a compromise solution was evolved and it was provided in the final version of the Companies Bill, 1953, that the administration of the Companies Act would be entrusted to a Department of Government functioning directly under the Minister in charge of the subject; but so far as the discretionary powers provided in that Act about management matters were concerned the Department would function only on the advice of an Advisory Commission to be specifically set up for this purpose. This was the genesis of the Company Law Advisory Commission constituted under section 410 of the Companies Act, 1956; as it stood at that time; (i.e., before the amendment of the Act in 1964) and its *raison d'etre.*

In this connection, it will be pertinent to reproduce the following extracts from the First Annual Report on the Working and Administration of the Companies Act, 1956, which brings out in clear terms the role assigned to the Company Law Advisory Commission:—

> **"The Commission is advisory in character, but in pursuance of the assurance given by then Finance Minister**

*Lok Sabha—7.9.55,—*vide* debates Vol. VII, No. 33, Column 12697.

to Parliament during the debates on the Companies Bill a convention has been established that all important cases where the views of the Department differ from those of the Commission, the relevant issues are referred to the Minister-in-charge before final decision is taken by Government on the Commission's recommendations. In fact, the Central Government has generally accepted the advice of the Commission in regard to the cases referred to them and has so far had not to differ from the Commission on any major issues of policy. The interposition of an Advisory Commission between the public and Government was considered desirable because of the large discretionary powers conferred on the Central Government under the different sections of the Act mentioned in section 411. It was felt that, in the exercise of these powers, Government should have the advantage of a careful assessment of the pros and cons of individual cases, which called for the exercise of Government's discretionary authority by a body of competent people, who were generally familiar with company methods and practices, and could be expected at the same time to take a broad view of the legal and social responsibility of company managements and also of the pervasive public interest implicit in the manner in which the companies carried on their work."

10.8. Provision was made in the Amending Act of 1964 for the establishment of an Advisory Committee to replace the old Company Law Advisory Commission. This Committee was, however, set up after some considerable time. We are not sure, if, in its present form, this Advisory Committee will possess the authority enjoyed by the old Company Law Advisory Commission or would be able to inspire the confidence which its predecessor was expected to do. The present Advisory Committee has no original powers of its own derived from the statute and can deal with only such matters as may be referred to it by Government.

We are, therefore, of the view that if the Administration of the Companies Act cannot be entrusted to a high-power statutory Authority or Commission of the type envisaged by the Bhabha Committee, the least that Government should do would be to endow the present Advisory Committee set up under section 410 of the Companies Act, 1956, with powers and responsibilities in respect of those areas where the Administration now exercises wide discretionary authority in regard to many aspects of company management and practice.

While there was full agreement in the Working Group as to the need for setting up an Advisory Committee or Commission carrying the requisite authority, with clearly defined powers and responsibilities, there was a difference of opinion among the members as to the procedure to be followed by this body in future. A majority of the members thought that it should be obligatory for Government to consult this Committee or Commission in regard to the formulation of *general* principles and guidelines in respect of the following matters:—

(1) Managerial appointments and remuneration;
(2) Removal of managerial personnel;
(3) Sole selling agents;
(4) Inter-company investments and loans;
(5) Inspections and investigations;
(6) Cost audit and special audit;
(7) Disclosures required in prospectus;
(8) Exemption of Government companies under section 620;
(9) Desirable debt, equity ratios;
(10) Amendment of Schedules;
(11) Any other matters referred by Government.

They did not, however, consider that it should be necessary for Government to seek its advice on indivdual cases, so long as decisions on them were taken within the limits of the guidelines approved by it, although they agreed that Government should be under an obligation to consult this body even in individual cases where the decisions on such cases went beyond the general principles and guide lines. In the thinking of these members this arrangement would avoid delay and the blurring of executve responsibility for decisions on individual cases. The Chairman of the Group on the other hand felt that it was necessary to distinguish between consultation/advice in respect of technical or quasi-technical problems and in respect of the exercise of discretionary executive powers in individual cases within the limits of the provisions of law and the administrative instructions issued by Government. In his view these two types of functions called for different types of Advisory Committee/ Commission. In the former case what was needed was a technically or professionally expert body; in the latter case no such technical or professional expertise was essential. The old Company Law Advisory Commission which was a statutory body was intended for the latter purpose, i.e., to assist the Administration in taking executive decisions on individual cases where under the provisions of the Companies Act the prior approval of Government was needed in certain areas of company management or company practice. The Chairman of the Working

Group felt that it was not proper to combine these two functions in one body and so far as the use of discretionary powers by the Administration was concerned, the duties and responsibilities of the proposed statutory Advisory Committee/Commission should be confined only to those sections of the Companies Act which conferred wide executive discretion on Government in dealing with individual cases. In his view no workable general principles or guidelines could be formulated in practice for this purpose which did not confer an appreciable measure of discretion on the Administration within their broad framework. It was therefore, a valuable safeguard to all concerned, to the business community as much as to the civil servants concerned with the exercise of these discretionary powers, if decisions involving the use of such powers were taken on the considered advice of a body outside the Administration. As regards possible delays in the taking of decisions, the Chairman of the Group considered that the record of the old Company Law Advisory Commission did not warrant the fears expressed on this score, and in any case suitable directions on this point could be issued to this authority by Government if this was necessary to do so. Nor did he see that there was any risk that the responsibility for decisions on individual cases which must necessarily devolve on the executive was likely to be blurred if individual cases were referred, for advice, to the Advisory Committee or Commission as they used to be in the past as long as the advisory character of the Committee/Commission was fully recognised by all concerned, and duly underscored by Government. Shri Kali Kukherjee was also inclined to this view.

All members of the Working Group were, however, agreed in emphasising the need for giving adequate publicity to the recommendations of the Commission, whatever they might be. Further, they also felt that reasons should be given for the decisions taken by the Commission or Committee on particular cases and where such decisions departed from earlier decisions, the jurisdiction for such deviation should be properly explained.

We trust that the recommendations that we have made in this Chapter will go far to mitigate the misgivings entertained in certain quarters about the manner in which individual cases are dealt with and would ensure that the discretionary powers of the Administration are exercised on the basis of relevant objective facts and primarily in the interest of the companies concerned and of the growth of sound company practice and behaviour.

CHAPTER XI

The present machinery for the Administration of the Companies Act.

In course of the preliminary studies leading to proposals for the comprehensive amendment of the Companies Act, in the years between 1950 and the final enactment of the Act of 1956, a great deal of thought was given to the appropriate form of organisation for the machinery for the administration of the new Companies Act. Much discussion took place on the comparative merits of different forms of organisation. Eventually, the debate was concentrated on the relative merits of the Statutory Authority or Commission and a departmental set-up, as examplified, respectively, by the Securities and Exchange Commission in U.S.A. and the pattern of the Board of Trade in the United Kingdom. The *pros* and *cons* of the argument were briefly summarised in the Report of the Expert Committee on the amendment of Company Law, 1952 (popularly known as the Bhabha Committee) and were considered at great length during the Parliamentary debates on the Companies Bill in 1954 and 1955.

11.2. In the previous chapter we indicated the reasons which eventually induced Government to opt for the departmental form of organisation. Although a section of the members of the Joint Committee of Parliament which considered the Companies Act was in favour of a high-power Statutory Commission, the majority of the members of this Committee endorsed the then Government's preference for a departmental set-up. The fundamental reason for this choice was that the new Company Law was no longer viewed, as it, traditionally, was in the past as primarily a lawyer's law, but was regarded as a basic measure of major socio-economic importance, which embodied not only some major issues of economic policy in its application to the corporate sector, but was also intended by Government to be used as an instrument of policy in furtherance of its economic and social objectives. This was the view of the new Company Law as it was finally accepted by Parliament. We quote the following extracts from a speech of the then Finance Minister, who was in charge of this Bill which will briefly explain the background of the decision then taken on this subject:—

(*) **"Government have, however, already accepted the recommendation of the Company Law Committee that**

(*) *Vide* Lokh Sabha Debate, dated 28th April, 1954, Vol. VI, No. 55.

the Central Government shall resume this responsibility for the administration of joint stock companies which it had delegated to the State Governments. This was the first necessary step in this scheme of our reorganisation. But, it was explained in the Statement of Objects and Reasons that although the Company Law Committee had recommended the establishment of a statutory authority at the centre, under the new Act, for the administration of the Company Law, and for the discharge of other related functions, for instance, capital issue control, regulation of stock exchanges, when a Central measure for this purpose was passed, Government considered that for the time being, at any rate, it was desirable to set up an organisation directly under the administrative control of the Government and to defer the conferment of statutory status on this organisation to a later date. In pursuance of this decision, a Central organisation has been set up under the Department of Economic Affairs. This organisation will have regional offices in important centres of trade and industry and will be in over-all charge of the administration of Companies Act through its regional offices. The Registrar of Joint Stock Companies will be under the direct control and guidance of this Central organisation. The organisation is now in the process of being built up and it is my hope that when it is fully established, it will constitute an important administrative reform and will be a major step in strengthening and improving the administration of the Companies Act all over India."

(@) "The real problem is the question of personnel. Whether you manage a thing departmentally, or whether you manage it through some statutory corporation, one need not assume that the proper personnel would be available. It is the man and not the machinery that matters. You may have all the apparatus of a statutory commission, and yet find that you cannot locate a proper person for guiding its affairs in which case you shall have gained nothing and indeed might have introduced complications; whereas if you manage departmentally, it is much easier to make changes in case such changes are called for. So these are the reasons, why we thought that at the moment the Central statutory authority should be a departmental body."

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(@) *Vide* Lok Sabha Debate, dated 3rd May, 1954, Vol. IV, No. 59.

(**) "The House might recall that in my speech moving for reference of the Bill to the Joint Committee, I had outlined the plans which I had in view for the administration of the Companies Act and related matters. I then explained why we had taken a provisional decision not to set up statutory commission as recommended by the Company Law Committee but had added that in this matter as in many others Government would be guided largely by the views of the Joint Committee. The subject was discussed at some length in the Committee and finally the Committee approved of the establishment of a strong central organisation for the administration of companies and related subjects. The Committee favours the establishment of a central department functioning directly under the Minister-in-charge and the more I think of it, the more I consider that it is a right decision. There are so many powers the exercise of which involves the decision of questions of policy and I cannot readily conceive of any statutory commission which is bound to be autonomous exercising these kinds of powers on behalf of Government, because their exercise goes to the root of the economic conditions in the country. Therefore, I think the House would approve of the arrangement recommended by the Joint Committee. They will be glad to know that we have already acted on this in advance of approval by the House and have set up a new department within the Ministry of Finance for this purpose. The responsibility of this department will include not only the administration of the Companies Act, but also such other institutions as are closely connected with the operation of companies, i.e., stock exchange, financial corporations, capital issue control, etc."

11.3. We have considered it desirable to reproduce at some length the extracts from the Parliamentary debates in 1954 and 1955, because we feel that they would explain better than we could the objects which the Government had in mind in preferring the departmental set up for the administration of the Companies Act to a Statutory Commission or Authority.

11.4. Nevertheless, in course of our enquiry, a strong view in favour of a high-power Statutory Commission or Authority was pressed on us by several witnesses. The consensus of opinion in our Committee was also in favour of such an organisation if the right type of people could be attracted to serve on

(**) *Vide* Lok Sabha Debate, dated 10th August, 1955, Vol. V, No. 13.

it. A few knowledgeable witnesses, however, felt that however desirable in theory a Statutory Commission or Authority might be, it would be extremely difficult for Government, in practice, to enlist the services of really competent persons of the requisite standing and status, who might be expected to serve on such a body for any length of time. In this view, they expressed the fear that such a statutory body if not duly constituted might end up by being manned by individuals of relatively junior status and standing in the middle ranks of the services or of trade and industry or of the professions connected with company management.

11.5. We further share the misgivings of these witnesses that the terms and conditions of appointment usually offered by Government might not attract men of competence and standing, outside limited governmental circles, even for such important positions as those of members of a high-power statutory Commission or Authority.

Nevertheless, we in the Working Group would prefer a statutory Commission of the type envisaged by the Bhabha Committee in its Report in 1952. The political and economic changes over the last few years under-score the necessity for insulating the administration of the Companies Act and related matters from the pulls and pressures of conflicting political and economic ideologies and placing it under the administrative control and guidance of an independent Commissionor Authority, consisting of competent persons from industry, trade, Administration and professions on a full-time basis. The need for this would be greater, if, as we recommend in a following chapter of our report, the administration of the Companies Act is also placed in charge of the same Ministry in the Government of India, as may be dealing with the other related measures and enactments like Capital Issue Control, Stock Exchange, Finance Corporations, etc.

If, however, Government do not consider it feasible to set up a high-power Statutory Commission or Authority which was recommended by the Bhabha Committee and which we still favocr, there is no other alternative but to fall back on a full-fledged Secretariat department which would make use of the services of experts from outside on contract basis.

11.6. In this context it is necessary to have a close look at the organisation now built up round the present Company Law Board.

11.7. The Department of Company Law Administration which had been constituted in 1955, was abolished at the end of October, 1963. In its place the administration of the Companies Act was entrusted to a Company Law Board created by the Companies (Amendment) Act, 1963, which started to function from February, 1964. Most of the powers and functions of the Central Government under the Companies Act were delegated to this Board. We have gone through the parliamentary discussions on this subject and also the Annual Reports of the Department. We have not been able to find any apparently satisfactory reasons for this drastic change in the then existing set-up. This Board was not correctly speaking, an independent high-power statutory Authority or Commission of the type, which either the Bhabha Committee envisaged or which we still consider to be a better form of organisation for the administration of the Companies Act and related matters. The Company Law Board as it was constituted in February, 1964, consisted of an Officer of Additional Secretary's rank together with the erstwhile Joint Secretary of the old Department of Company Law Administration, and was nothing more than a departmental Committee. In course of the debates in Parliament the then Minister in charge of this subject claimed that this Board was set up on the analogy of the Boards of Direct and Indirect Taxation, which had been carved out of the Central Board of Revenue, and that it would facilitate collective decision-making and thereby secure greater efficiency, cohesion and despatch the administration of the Companies Act—a claim which is again repeated in the Eighth Annual Report on the Working and Administration of the Companies Act. The circumstances in which the old Central Board of Revenue (since bifurcated into two Boards of Direct and Indirect Taxation), came into being many decades ago were entirely different from the circumstances in which the Company Law Board replaced the then existing Department of Company Law Administration. When the old Central Board of Revenue was set up, of which the present Boards of Direct and Indirect Taxation are lineal descendants, there was no secretariat department in the Government of India dealing with the administration of taxation matters. When the Company Law Board was set up in February; 1964; a full fledged secretariat department; viz., the Department of Company Law Administration was already in existence and had already built up the field offices of this Department and the methods and techniques of administration of the Companies Act in its specialised areas. Besides, there was no real analogy between the duties and functions of the Central Board of Revenue and those of the Company Law Board which was a purely administrative body. Further the argument about collective or rather collegiate decision-making by a Board consisting of a Senior Officer assisted by his junior colleagues was misleading and, indeed, confusing, inasmuch as: in practice; decisions in any secretariat Department are always

taken on the basis of consultations between its senior officers who are invariably involved in the decision-making process.

11.8. In this context we had an opportunity of studying a few notes prepared by the present Company Law Board for our information. It was clear from these notes that the manner in which the Board was functioning was, in no material particulars, different from the administrative methods followed in the old Department of Company Law Administration, or indeed from any other secretarial department. The substitution of the Company Law Board for a secretariat department in February, 1964 was, therefore, not only uncalled for but also served little useful purpose in practice.. In the circumstances, it was not surprising that the Minister-in-charge soon developed second thoughts on this subject and the Department of Company Law Administration was revived within a period of less than ten months from its abolition, *albeit* under a new name, viz., the Department of Company Affairs and the Chairman and members of the Company Law Board were formally re-designed as secretaries and joint secretaries of the new Department of Company Affairs and Insurance. In the light of this re-organisation of the administrative set up in the secretariat it is not clear why advantage was not taken of the amendment of the Companies Act, soon after this administrative re-organisation took place, to abolish the Company Law Board, so that its functions could be merged in the resurrected secretariat Department dealing with Company Affairs and Insurance and it need not have continued to co-exist with this Department as a subordinate appanage. This Board has now become virtually a 'fifth wheel' hardly contributing to the cohesion or despatch of business in the administration of the Companies Act.* On the contrary the continued existence of this oard with the frame-work of the Department of Company Affairs masks the true responsibility of the Department

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*Two of our colleagues who belong to the Department of Company Affairs, viz., Sarvshri S. Venkataraman, Director of Inspection and Investigation and P. B. Menon, Regional Director, Calcutta, expressed the desire that they should not be regarded as having associated themselves with the observation that the Company Law Board did not contribute to the cohesion or despatch of business in the administration of the Companies Act. They are of the ivew that so long as the law stands, as at present, there is no alternative but for the continuance of the Company Law Board and that there was no convincing evidence Board is "a fifth wheel hardly contirbuting to the cohesion or despatch tendered before the Group in support of the observations that the of business in the administration of the Companies Act. On the contrary, the continued existence of this Board with the frame-work of the Department of Company Affairs masks the true responsibility of Department and particularly of the Minister-in-charge and renders constitutional accountability for decisions taken by the Board needlessly confusing and, in part deceptive." As such, they have not agreed with the recommendations at the end of paragraph 11.7 and they have signed this report subject to this reservation.

and particularly of the Minister in charge, and renders constitutional accountability for decisions **taken by the Board** needlessly confusing and, in part, deceptive. Having regard to these facts,

We consider that it will be a major step towards streamlining the present organisation for the administration of the Companies Act and related matters at the top level, if the Company Law Board which has no longer any special functions to discharge is wound up and the responsibility for the administration of this Act is placed squarely and visibly on the Department of Company Affairs.

11.9. This rationalisation of the administrative set up will also reduce a good deal of unnecessary clerical work and needless duplication of notings in the secretariat as between the Company Law Board and the Department of Company Affairs and the vice versa.

11.10. We now turn to the regional and state organisations of the Department of Company Affairs. The present regional and state set-up represents basically the same administrative pattern as was set up in 1955-56, when the Department of Company Law Administration was constituted.

From the evidence that we received at all the leading centres of trade and industry, it was clear that this pattern of organisation was considered suitable and adequate for the enforcement of the Companies Act. We have no doubt that with appropriate reinforcements of staff strength at the technical levels, the Regional Directorates and the offices of the Registrars in the States would be able to cope with the additional work which they may be called upon to handle when other related subjects like Capital Issues Control, Stock Exchange, Finance Corporations and few other measures and enactments to which we refer in the following chapter are also transferred to the Department responsible for the administration of the Companies Act.

11.11. In this context the specific suggestions contained in the following paragraphs were made by several witnesses.

11.12. *In the first place*, it was suggested that an Additional Directorate should be created to deal with the rapidly increasing volume of work in some of the northern and central states which have been hitherto somewhat industrially backward. In

this connection our attention has been drawn to the regional set-up of the Department in 1955-56, which then consisted of five Regional Directors instead of four, as at present, with headquarters at Bombay, Calcutta, Madras, Delhi and Kanpur. It is not clear to us why within a few months of the establishment of these regions one of the northern regional offices was suddenly abolished.

We, therefore, concur in the suggestion made and recommend that the present northern region be bifurcated into two Directorates—one with its headquarters at Kanpur as at present and the other with its headquarters at Delhi. The Regional Director of Kanpur has at present a very large geographical area, which is also relatively under-developed, under his charge and if this extensive area is to be properly looked after, it is necessary to create another Regional Directorate.*

11.13. The Kanpur Regional Directorate should include within its jurisdiction the States of U.P., Madhya Pradesh and Rajasthan while the jurisdiction of the Delhi Directorate should include the States of Punjab, Haryana, and the Union Territories of Himachal Pradesh and Delhi. If and when the Companies Act, 1956, is extended to the State of Jammu and Kashmir, the Delhi Directorate should also take charge of it.

11.14. *A second suggestion* which had the support of many competent witnesses, including the representatives of some of the leading Chambers of trade and industry concerns the delegation of further powers under the Companies Act to the Regional Directors. Witnesses referred *inter alia* to the following sections of the Act:—

Section 8: Power to declare that an establishment shall not be treated as a branch office.

Section 20: Power to declare the name of a company to be undesirable.

[It may be noted in this connection that the powers under sections 21 and 22 to approve of changes in the names of a company and to rectify the names of companies have been already delegated to the Regional Directors.]

*One of our members, Dr. R. K. Hazari, considered that it was not necessary to create this additional Directorate in view of the relatively small number of companies existing in this region. Another member, Shri Kali Mukherjee, thought that this additional Directorate should be set up only when the Administration felt that it was necessary to do so.

Section 108: Power to extend the period within which the registration of transfer of shares is to be effected.

Section 111(3): Power to hear appeal regarding refusal to register, transfer or transmission of shares.

Section 149(2)(b): Power to allow commencement of new business where only an ordinary resolution is passed.

Section 211(4): Power to sanction, modification of forms of balance sheet.

Section 213: Power to extend the date of the financial year, Annual Returns and general meeting of a holding company so as to make it coincide with the financial year of its subsidiary.

Section 295: Loans to directors.

[Subject to such detailed policy instructions as might be given by the Department of Company Affairs.]

Section 283(i)(f): Power to remove the disqualification incurred by a director failing to pay any call in respect of the shares held by him within six months from the date fixed for the payment of call.

[Subject to specific instructions to be laid down by the Department of Company Affairs.]

Section 300(3): Power to exempt a company director from participating or voting in a Board's proceedings where contracts in which he is interested are discussed.

11.15. The above suggestions for the decentralisation of powers under the Companies Act to the Regional Directors are only illustrative. Our view on this suggestion is that where such powers affect the day-to-day work of companies and do not involve any major departure from the basic policies embodied in the Act or in well-established company practice, it would be an advantage alike to the Administration and to the business community to delegate these powers to the Regional Directors. For, they would be able to deal with the local businessmen more conveniently than the Department of Company Affairs situated in New Delhi could do.

In this light of our general view on this subject we suggest that a departmental committee under the Chairmanship of the Secretary of the Department of Company Affairs should go into this subject and prepare

a scheme of further delegation of powers to the Regional Directors without delay. This delegation will not present any legal difficulty but will involve only a simple administrative decision.

11.16. A third suggestion concerns the powers vested in the courts of law. We agree that some of these powers could also be advantageously transferred to the Regional Directors. We mention a few of them, again, by way of illustration only:—

Section 17: Amendment of the Memorandum of Association of a company.

[Subject to such guiding principles as the Department of Company Affairs might lay down.]

Section 141: Rectification of the Register of Charges and extension of time for registration.

Section 163(vi): Order compelling immediate inspection of documents when refused.

Section 234-A: Sanction to the Registrar of Companies for seizure of company records.

[On the lines of similar powers given to Collector of Customs under the Customs Act.]

Section 240-A: Sanction to Inspectors for seizure of records.

[Similar to powers given to the Collector of Customs under the Customs Act.]

11.17. In regard to the last two sections mentioned above, the Department of Company Affairs may lay down detailed guidelines for the use of Regional Directors and further require that a short statement of cases should be sent to the Department before the necessary sanction to the Registrars and Inspectors is given. An amendment of the Act would be needed to give effect to our suggestion so far as the transfer of powers from the courts to the regional Directors are concerned. That should provide all those interested in or concerned with this subject with a reasonable opportunity for debating the issue of policy involved in our recommendations

11.18. *A fourth major point* regarding the Administration of the Act in the Regional Directorates and in the Offices of Registrars which was brought to our notice by many witnesses was the need, alike for improving the quality, at key points, of the staff employed in their offices and for re-inforcement of the existing staff strength particularly in the legal and accounting

sections of these Offices. If our recommendation for unified administration of the Companies Act and other related subjects, to which we refer in chapter XII of this report and the establishment of a comprehensive Ministry at the Centre, dealing with all these subjects is accepted, we anticipate an appreciable addition to the load of work in the Offices of Regional Directors and Registrars of Joint Stock Companies, particularly at the higher levels. These offices will in that event require not merely some quantitative addition to their staff strength but also a better calibre of personnel in their higher ranks. . Further, if the administrative responsibility for supervising the work of the Official Liquidators is to be increasingly transferred from the courts to the Regional Directors, this will also call for a sizeable strengthening of the staff strength in the regional offices of the requisite competence. This again is a subject which has to be examined, in some depth, on the basis of facts and figures and the relevant statistics relating to the existing staff strength in these offices.

It is important that this study should be undertaken by a high-power departmental committee under the Chairmanship of the Secretary of the Department as soon as a decision on the major policy issues raised by us has been taken. We understand that the Department of Company Affairs is now more than self-supporting and that its fee-income much exceeds the expenditure incurred on this Department. In this connection we fully endorse the observations of the Estimates Committee of Parliament contained in their 53rd Report, 1963-64, in which they commented on the excess fee-earnings of the Department and suggested that as the amount of fees realised from the joint stock companies during the previous three years had far exceeded the amount of expenditure on the administration of the companies Act, the question of, crediting the excess revenue to a special fund for the purpose of undertaking research in corporate matters and in imparting training to company accountants, company secretaries, etc. might be examined. The expenditure on the additional staff strength which we have suggested for the offices of the Regional Directors and the Registrars would be a legitimate charge on the surplus of fee-income earned by the Department.

11.19. We, therefore, hope that the cost of our proposals would not be argued as an impediment to their implementation, so far as the Department of Company Affairs at any rate is concerned.

Closely allied to the question of staff strength is that of improving the quality of the officers and the senior staff not only in the Regional and the Registrars

Offices but also at the headquarters of the Department of Company Affairs itself. If the Department and its regional and state offices are to be fully prepared for and geared to the additional responsibilities which we visualise for them, it is essential that arrangements for systematic periodical in service training and orientation courses for the officers and staff of the Department should be made.

11.20. The senior officers of the Administration should consider this to be a very important part of their duties and responsibilities, and should be prepared to devote some of their time to this matter. It may be worthwhile for them to obtain the technical advice of the established professional institutions like the Institutes of Management at Ahmedabad and Calcutta and the Staff College at Hyderabad, to mention only a few of the more important professional bodies concerned with the problems of the management of joint stock enterprises. We have no doubt that these institutions will be ready to offer their advice not merely on the design of the training and orientation courses, but would be also ready to undertake the running of some of these courses, with the active help and co-operation of the senior officers of the Administration.

At an earlier stage in the history of the Department of Company Affairs, a close link had been forged between the then Department of Company Law Administration and these Institutes and some private commercial training institutes in Bombay and Madras. These links should be revived and a continuing system of training and periodical orientation course should be organised and programmed for.

11.21. A Bureau of Public Enterprises has been recently set up by the Government of India in the Ministry of Finance. We were given to understand by official witnesses that the duties of this Bureau will include the recruitment and placing of managerial, legal and accounting personnel in the public sector undertakings of the Central Government. We welcome this more as we consider it as a major step towards the efforts that are now being made to systematise appointments to the top posts in public undertakings by drawing up panels from all available fields.

So far as the managerial personnel needed for these undertakings is concerned, we consider that there is need for close collaboration between the Department of Company Affairs and the Bureau of Public Enterprises.

11.22 If our recommendation for a comprehensive Central Ministry to deal with the Companies Act and all other related subject is accepted by Goernment, the need for such collaboration would be inescapable.

It is not enough that the Secretary or some other senior officer of the Department of Company Affairs is a member of the Co-ordinating Committee which functions as the governing body if the Bureau of Public Enterprises. It is also necessary that the work of the Bureau in regard to the recruitment, training and placing of managerial, legal and accounting personnel of companies is closely integrated with the activities of the Department of Company Affairs in this area. This Department is closely connected with the professions of the Company lawyers and company accountants and also with the problems of management of companies and should be in a position to offer the necessary technical advice and guidance to the Bureau in the formulation of its plans and programmes in regard to the recruitment and training of specialised managerial personnel concerned with management.

In this context, we reproduce the following extracts from the Reports of the Estimates Committee for the year 1955-56 on the Ministry of Home Affairs (Public Services):—

"They (the Committee) need hardly stress that in the analysis the succes of an individual is largely determined by the kind of leadership which is provided by the top echelon of service.

The Committee suggest that suitable arrangements should be made for providing an intensive course of training to officers who are deputed for the first time to public undertaking, in fundamentals of business and industrial management, with special reference to management accountancy, organisation and methods and the inter-relation between production and sale.

The deputation to public undertakings should not be allowed to become merely a rung in the steeplechase for higher and higher scales of pay and allowances for officers but should be based on a careful matching of the aptitude and proven ability of an officer within the known requirements of an undertaking."

One aspect of the type of integration between the Bureau of Public Enterprises and the Department of Company Affairs which strikes us as being full of administrative potentialities is the better utilization of the accounting, legal, financing and other experts who are now in the Company Law Board Service, public enterprises and also in other branches of Administration.

CHAPTER—XII

Integrated administration of Company Law and related enactments

In the previous chapter we have dealt with the organisation and structure of the present machinery for the administration of Company Law, and have also considered some major problems relating to the staffing of the central, regional and field offices of the Department of Company Affairs which, in our view, have a direct bearing on the efficient and expeditious administration of the Act. We have also stressed the need for systematic, periodical in-service training and orientation courses for the benefit of officers and staff of the Department, so that they can keep themselves abreast of the rapid changes that are taking place in the organisation and working of joint stock enterprises and may be in a better position to appreciate the economic and social forces motivating them. In this Chapter, we propose to consider another major organisational and administrative problem, which, in our view, is as important as the issues which we discussed in the previous chapter. The effectiveness of the administration of Company Law, not merely in the narrow technical sense, but in the wider sense of helping to achieve aims and objects of the legislation would depend not merely on the efficiency of the administrative machinery entrusted with the responsibility for its administration, but also on its scope and range, and on the degree of coordination which this machinery can bring about between its work and the policies followed by other agencies in administering other related measures, which have a close bearing on the the working of the corporate sector. The need for such coordination and integration of the administration of Company Law with the other enactments which are now being administered by other agencies was recognised as early as 1952 when the Expert Committee on the amendment of Company Law (popularly known as the Bhabha Committee) submitted its report. We need only quote the following few sentences from paragraph 257 of that report : "We are, therefore, strongly in favour of a statutory authority for this purpose. This does not mean that the Central Authority* would function in isolation

*The reference is to the strong preference of the Bhabha Committee for a statutory body to deal with the administration of the Companies Act and all other related measures as against a purely departmental organisation, which was, however, favoured by Government at that time and was subsequently set up.

from the main currents of economic policy that may be adopted by the Government of the day. Clearly, major issues of economic policy relating to the private sector of the country's economy, in so far as they bear on the working of the companies must ultimately be matters for Government although we visualise that the Central authority along with others would be closely connected with the formation of such policy in its formulative stages. But once these issues of economic policy have been settled and embodied in legislative or executive decisions, the application of the accepted principles to individual companies whether in respect of their formation or working, should be the responsibility of a quasi-independent authority....."* Further, in the course of the report, while detailing the functions proposed for the Central Authority, the Committee added specifically that this body "should also keep the investment markets in the private sector of the economy under continuous observation ..... the Commission should also carry on such other functions relating to capital issues control regulation of stock exchanges and any other subject connected with the promotion and formation of Joint Stock companies which the Central Government may delegate to it....."**

12.2. In partial modification of the recommendations of this Committee the Government of India set up in 1955, a secretariat department called the Department of Company Law Administration instead of a central statutory commission, but with a wide range of functions directly concerned with the working of the corporate sector as had been suggested by the Bhabha Committee. Subsequently, a Joint Committee of Parliament endorsed this decision of Government. In the result, the duties and responsibilities of the Department in the initial years included not only the administration of (a) the Companies Act, but also of (b) capital issue control, (c) stock exchanges, (d) financial corporations, including the Industrial Finance Corporation, the State Finance Corporations, the Industrial Credit and Investment Corporation of India and the then existing Rehabilitation Finance Administration and lastly (e) the profession of accountancy.

12.3. We do not wish to pursue at any length the numerous shifts in administrative policy, not easy to explain in rational terms, which followed one after another between 1956 and 1965; as a result of which some of the subjects which had been allotted to the then Department of Company Law Administration (since renamed Department of Company Affairs) were taken out of this Department and transferred to the old Department of

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Vide pages 193-194 of the Report of the Company Law Committee. 1952.

**Vide* page 196 of the Report of the Company Law Committee 1952.

Economic Affairs, although at a later date again, a few of these subjects were re-allotted to the Department of Company Affairs. It will be unprofitable to comment on the aberrations of policy which were responsible for this inexplicable administrative confusion during the few years, but responsible informed opinion has always strongly stressed the necessity of co-ordinated and integrated administration of the subjects listed above under one departmental roof. We need only quote the observations of the Vivian Bose Inquiry Commission, which, on the basis of a detailed analysis of company mal-practices and company mismanagement on a large scale in the Dalmia group of companies came to the finding that in the interest of the efficient and effective regulation of joint stock companies, it was essential that several other enactments and institutions which were directly concerned with company management, should be administered by the same authority as was in charge of the administration of the Company Law, We quote the following lines from the report of that Commission:

> "..... The Commission would wish Government to consider one important issue relating to the organisation and working of the various departments of Government which are at present dealing with the corporate sector. The Department of Company Law Administration (now the Department of Company Affairs) deals generally with the working of Companies Act, ensures its compliance and is regulating authority where Central Government sanction is necessary under various Sections of the Act; but there are other departments which deal with different aspects of the matter, such as the control over capital issues, Stock Exchange regulation, etc. These departments come under a Ministry, different from the Ministry under which the Department of Company Law functions, and the Commission feels, as the Bhabha Committee did, that there is need for integrated administration of the Companies Act as well as other matters connected with the corporate sector."*

12.4. A large number of witnesses who appeared before us on behalf of many different organisations and institutions connected with the working of joint stock companies expressed themselves equally strongly on this subject. The great majority of them were of the view that it was essential in the interests of the Administration as well as the business community that

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Vide pp. 813-14 of the Report of the Vivian Bose Commission of inquiry (1962).

the subjects to which we have referred above should be dealt within one government department.

We concur in this view, and are convinced that the case for bringing all these related subject under one Administrative roof is so overwhelming that any marginal advantages which now accrue to some of the secretariat departments from the present haphazard distribution of subjects among them are more than offset by the serious damages caused to the administrative effectiveness of these measures by their fractionated administration in different ministries. Government can never expect to produce any impact on the corporate sector if different governmental or quasi-governmental agencies continue to pull at each other and fail to evolve a coordinated and integrated policy under which alone the different types of administrative weapons in the department armouries of Government can be wielded purposefully for the purpose of achieving the common objects and goals of all these agencies.

12.5. The arguments in favour of the integrated administration of several of the subjects listed above are so obvious that we do not wish to dilate on them but for the sake of the fullness of the narrative would only touch on them. Under present day conditions, capital issue control is now largely an exercise of control over the capital structure and the terms of incorporation of companies, i.e., over the technical conditions of the issue of capital, and is intended primarily to ensure a healthy and balanced capital structure for companies, subject to the broad priorities of industrial development as laid down in our Plans. It has very little to do with the problem of inflation, which originally gave birth to this Control or with the Control over foreign investments, in regard to which it was an important instrument of policy, before the present elaborate apparatus for the regulation of foreign investments was devised or, indeed, with any other major issue of economic policy.

12.6. The inter-relation between joint stock companies and stock exchanges is equally intimate. Indeed for many years prior to 1951, joint stock companies and stock exchanges were under the administrative responsibility of the former Ministry of Commerce. The market for new issues of capital provided by a regulated stock exchange and the terms and conditions on which the operations in this market can be conducted are matters of vital importance to the extension and development of joint stock enterprises. The apparatus and the institutions of the new issue market in particular are closely connected with the working of the Companies Act and indeed Part IV of the Companies Act deals with matters which specially concern these institutions. The regulation of broker-dealer

relations vis-a-vis the investors is another important function of the stock exchange which is of great importance to the conduct of the business of companies. All these facilities which these stock exchanges offer are liable to abuse. It is, therefore, additionally important that the administrative authority which deals with joint stock companies should also be in administrative charge of stock exchanges. Many witnesses specifically brought to our notice the difficulties caused to brokers as well as their clients including the joint stock companies by the absence of any adequate co-ordination between the Department of Company Affairs and the Department concerned with the administration of the stock exchanges.

12.7. The inter-relations between joint stock companies and the financial corporations and other financial institutions operating in the private sector, e.g., the Industrial Finance Corporation and the State Financial Corporations, the National Industrial Development Corporation, the Small Industries Credit Corporation, the Industrial Development Bank, etc. are too obvious to require much elaboration. What the sound and efficient working of these institutions requires is competent and detailed knowledge of the structure and mechanics of company management and not merely general knowledge of the industrial or commercial policies of Government, or of the priorities to be given to companies seeking financial accommodation or assistance from these finance and investment corporations under our Five-Year Plans. There must, therefore, be the closest liaison between the operations of these financial institutions and the administration of joint stock companies. This will ensure not only efficient working of the financial institutions by placing at their disposal valuable inside information about the working of companies and about the operations of powerful business groups but will also strengthen company administration by placing at its disposal equally valuable information about the resources deployed by these groups and the manner of their deployment. If responsibility for the administration of the Companies Act and that of the financial corporation and financial institutions mentioned above continues to remain dispersed as at present and no attempt is made to bring these institutions which now function in separate water-tight compartments under one and the same administrative roof, it would be impossible to secure the integrated and purposive regulation of the corporate sector.

12.8. For many years past in the Government of India, the subject of Company Law, Stock Exchanges and Insurance were under the administrative supervision and control of one and the same Ministry, namely, the Ministry of Commerce. When these subjects were transferred from that Ministry to the Ministry of Finance, all these subjects were eventually brought under

one Department in the latter Ministry, namely, the Department of Company Law Administration which also dealt with the financial institutions including the Industrial Finance Corportion and the Industrial Credit and Investment Corporation. The administrative responsibility for the Life Insurance Corporation was, however, kept apart. Although the intention at that time was that as soon as the Life Insurance Corporation had been fully organised after the nationalisation of Life Insurance companies in the private sector, the subject of Insurance would be re-transferred to the same administrative department, i.e., the Department of Company Law Administration which was dealing with the other related subjects, namely, Capital Issue Control, Stock Exchanges and the financial corporations. The L.I.C. enquiry (popularly known as the Chagla Enquiry) in 1957-58 once again drew attention to the conflicts of policy and administration which might follow from the existing divorce of the responsibility for dealing with the problems of company finance and company investment from that of company management. Unfortunately, no steps were taken to bring about the desired reorganisation in the secretariat departments till 1960, when by a Presidential Order, dated the 18th November; 1964, the subject of Insurance was again brought under the Department of Company Affairs. This was, however, a short-lived reconciliation. The aberrations of administrative policy to which we referred earlier again separated this subject from the then Department of Company Affairs in January, 1966. We need hardly comment on these changes of shuttle-cock frequency in the organisation of secretariat departments which took little note of the essential requirements of purposive and integrated administration of subjects closely linked to one another.

12.9. We had the advantage of examining a Deputy Governor of the R.B.I., who was in charge of industrial financing, the Chairman of the L.I.C. and the Chairman of the Unit Trust of India, besides representatives of the Stock Exchanges and discussing with them the need for an integrated Department of Company Affairs which would be concerned not only with the organisation and working of joint stock companies, but also with the working of the related financial institutions catering to the financial needs of companies besides L.I.C. and the Unit Trust of India. While there was general agreement that both in the formulation and execution of policies, all these institutions must function in a co-ordinated manner, and that there should be systematic and frequent consultation among them not only at the headquarters of these organisations, but also at their regional offices, there was no similar agreement as to the secretariat ministry under the administrative supervision and control of which all these subjects should be brought together.

12.10 We have given this subject considerable thought. While we do not feel called upon to pronounce on the claims of any of the existing Ministries to these subjects,

We are convinced that in the interest of the efficient and purposive administration of not only the Companies Act but also of the other related eactments dealing with the stock exchanges, the Industrial financial corporations, the Life Insurance Corporation and the Unit Trust, all these institutions must be administered under the broad policy guidance of one and the same Ministry.

12.11. At present it was difficult for the authorities of these institutions to take any comprehensive view of their duties and responsibilities, bearing in mind not only the aims and objects underlying the various regulator measures but also their basic logic. This was clear from the testimony of the heads of these institutions. The line taken by them, generally, was that it was their duty to administer these institutions primarily in the light of the provisions of their constitutent laws, and so far as the general economic policy of Government in its application to these institutions was concerned, it was for Government, through the administrative departments concerned, to indicate to them precisely the directions in which the financial policies of these institutions needed modifications. This view explained why in practice these institutions had always adopted a somewhat detached and neutralist attitude towards the economic and social consequences of their investment decisions. This attitude is of course, in line with the earlier traditional policy and practice of similar institutions and agencies in Britain from which it appears to have been inherited by the heads and senior officers of our financial institutions. But this attitude is fast changing even in that country. Although in the past the comparable British institutions always tended to be passive investors and not active representatives of the shareholders' interest, both pressure from outside and the internal developments of these institutions themselves are bringing about a rapid transformation in their thinking on investment policies and attitudes. As two competent observers in that country have recently recorded:—

> "More and more shareholders are beginning to look to the institutions for a lead. Indeed, they are in danger of being accused of doing too little rather than too much ..... the disappearance of the wealthy individual investor, powerful enough to make a fuss, doubles the responsibility of the individual investor.".*
> and again

*Mr. A. Bambridge, "The Reluctant Puppet-Masters" in the Observer July 23, 1967.

"The national interest in calling inefficient managements to acount points the same way. Meanwhile, a growing number of the institutions themselves are finding that, with their increasing involvement in equity shares in general, and in particular companies, the least expensive way to protect their own interests and improve their profits is to intervene to improve efficiency, and to acquire the staff needed for this, rather than to risk damaging the market by simply disposing of important blocks of unprofitable shares."**

We consider that the authorities of all these institutions should try to evolve a comprehensive and coherent policy as to their duties and responsibilities as important shareholders in the large number of joint stock companies in which they invest their funds.

12.13. To particularise, problems such as the manner in which the corporations should exercise their rights and duties when the affairs of a company in which they have a financial stake do not appear to go as well as they should; the attitude which they should adopt towards demands for inspection and investigation into the working of particular companies or as towards demands for changes in the control of such companies (e.g., the manner in which these corporations should conduct themselves at the general meetings of companies where they had a leading role to play by virtue of their position as leading shareholders); the attitude which they should adopt towards the demands increasingly made on the companies not only by their own managers, but also by the local community and the general public; their attitude towards expenditure in research and development by the companies in which they are interested—do not as yet appear to receive such careful consideration as they deserve from the authorities of all these institutions, including the Unit Trust of India.

We are clear in our mind that it would not be feasible for them to take the desired intiative in regard to all these matters, much less to evolve common and concerted policies, fitting into their operational methods and practices, unless all of them are brought under the administrative policy guidance of one and the same Ministry in the Government of India. We,

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****Vide** Prof. Michael Fogarty in P. E. P. broadsheet on "A Companies Act, 1970"—1967, p. 107.

therefore, strongly recommend that all these subjects and agencies should be brought under one administrative roof in the Central Secretariat without avoidable delay.

12.14. Incidentally, an additional advantage of the type of co-ordinated and integrated administration of these closely related subjects which we propose would be to raise the quality of the administration of all these individual agencies through the processes of mutual consultation and the cross-fertiliation of inter-ccmmunication. In other words, the managers and senior officers of these institutions will learn to deal with the subjects entrusted to their care not merely as specialised crafts, but as significant economic and social institutions with enormous potentialities for good for the behaviour pattern of our joint stock enterprsies.

When the integrated Ministry which we recommended has been set up, Government should also consider the desirability of transferring to it those provisions of the Industrial (Development and Regulation) Act, which deal with the investigation of companies in distress.

12.15. Nothing would be gained by keeping these essential management problems, whatever might have been proximate causes of the failure of such companies, from the Ministry which is primarily concerned with the organisation, structure and working of joint stock companies.

Similarly, the laws which deal with the organization, structure and management of other institutions, e.g. , the provisions of the Banking Laws (Miscellaneous Provisions) Act relating to the management of commercial banks and banking institutions, should also be administrated in close consultation and collaboration with this Ministry, so that, as far as possible, uniform regulatory policies in regard to the structures and functions of all joint stock companies may be evolved and unnecessary duplication of regulatory work in the different Ministries may be avoided.

12.16. We recogngize that any attempt to reorganize the working of these different institutions and agencies in the manner proposed by us will encounter special difficulties in decision-making in a relatively sensitive area of secretariat re-organisation and may thereby delay the establishment of the unified and integrated Ministry which we have recommended

12.17. We, therefore, suggest that pending consideration of this recommendation, Government should forthwith

initiate measures to provide for the maximum possible degree of consultation and co-ordination in the working of these institutions and agencies, in a more meaningful and purposive manner than they have been administered so far. This can be done by the establishment of inter-departmental standing committees both at the headquarters and the regional offices of these different institutions and agencies, in all important commercial areas of this country, and to a limited extent, by the inter-change of personnel among these institutions whenever opportunities for such interchange arise. The duties and re ponsibilities of the suggested standing committees should be laid down with reasonable precision, and the heads of these institutions should be encouraged in associate with one another freely, as administrative experts and specialists, without being hindered by their departmental or ministerial attachments.

12.18. This is one of our major recommendations that are based on a very wide measure of agreement among the leading non-official witnesses, who appeared before us. One special point which all of them made was that, apart from the gain which such co-ordinated and integrated administration of related subjects would bring to Administration itself, from the point of view of public relations also this administrative reorganisation would prove to be a much needed reform. The business community and the public, we are told, would welcome any such measure. For it would help greatly to reduce, if not altogether to eliminate, the present, administrative delays, inescapable from seemingly never-ending inter-departmental consultations and the circulation of notes and files among different Ministries.

CHAPTER XIII

Winding up of Companies.

I

The traditionally neglected subject of the liquidation of companies has not been specifically included in our terms of reference but it constitutes the most unadministered sector of the Companies Act. The loss of corporate wealth and income which the shells of defunct companies conceals is, in a sense, a national waste and the longer the winding-up proceedings in respect of such companies continue, the greater is the loss to the community, Liquidation procedure is, more or less, analogous to the administration of the estate of a deceased person; but the process is distinguishable in that in a winding-up proceeding the defunct company continues to survive, although in a comatose state till it is mercifully put to death when the company is finally dissolved. The administration of assets and liabilities in this case precedes the extinguishment of life and not *vice versa*, as in that of the estate of a deceased person. We have, therefore, considered it a sufficiently important topic to discuss it in this chapter. Several witnesses and the full time Official Liquidators attached to the High Courts especially of Bombay, Calcutta and Madras, brought to our notice several difficult administrative problems involved in the winding-up proceedings which need early attention.

13.2. We were told that as on 31st December, 1965, 2,559 companies were under liquidation. Of these, 1,030 companies representing 40.2 per cent of the total were under winding up, by the Court; 1497 companies were under voluntary winding up, and 32 companies were under winding up under the Court's supervision.

13.3. Out of the total number of companies under winding-up by the Court, 200 were under liquidation for five years or less; 262 between 5 and 10 years: 355 between 10 and 15 years; 165 between 15 and 20 years; 16 between 20 and 25 years; 22 between 25 and 30 years; 8 between 30 and 35 years, and 2 for over 35 years. It will be seen from these figures that a very large number of companies are under winding-up for periods exceedng five years.

13.4. The Companies Act, 1913, which preceded the Act of 1956 provided more or less for the exclusive control of the liquidation proceedings by the Court, the Government hardly

intervening in them except in rare cases. The Courts were free to choose the persons by whom the administration of companies ordered to be wound-up was to be carried on. These individual liquidators carried on their work ostensibly under the control and guidance of the Courts but in practice there was hardly any supervision over the work of the former or any attempt to systematise the procedure to be adopted by them. In many cases, after passing the orders of winding-up, the High Courts transferred the proceedings to the District Courts for further hearing. The High Courts were free to formulate the rules applicable to the winding up proceedings within their jurisdiction, with the result that there was no uniform procedure applicable to all companies on an All-India basis. The periodical statements of accounts required to be filed by the Official Liquidadators with the Court as well as the Registrar of Companies, were not sufficient protection to the creditors and the contributories. Indeed it might not be far from the truth to state that in many cases the liquidation proceedings were seemingly conducted more for the benefit of the liquidators themselves than for the creditors or contributories of the companies concerned.

13.5. The Government, was, therefore, anxious that this state of affairs should come to an end and that adequate administrative control and supervision of winding up proceedings should be enforced. With this object in view, the Companies Act, 1956 introduced two important administrative changes. The first was the appointment of full-time or part-time Official Liquidation, who were to be attached to the High Courts by the Central Government under Section 448 of the Act and to be entrusted with liquidation of companies within the jurisdiction of such High Courts. The authority of the High Court to appoint any person as an Official Liquidator in a winding-up proceeding which was available under the provisions of the Indian Companies Act, 1913 was thus withdrawn. In accordance with the provisions of Section 449 of the 1956 Act, the officers appointed by the Central Government under section 448 of the Act were automatically to become the official liquidators of companies ordered to be wound up by the Court. The other important provision for the exercise of administrative control and supervision by the Central Government over liquidator's work in respect of administrative matters was section 463 of the Act under which, for the first time, the Central Government was empowered to take cognizance of the work of official liquidators. This was followed by an amendment of Section 515 of the Companies Act, by which the Court on a suitable application being made to it and on being satisfied that a voluntary liquidator was not carrying on his duties properly, could remove him and appoint a new voluntary liquidator or direct the official liquidator to take charge of the liquidation proceedings. The intention underlying these provisions was clearly to ensure that, in addition to the judicial supervision exercised over their judicial work by the Court, the liquidators

should also be subjected to the broad administrative supervision of Central Government. The power conferred on the Central Government in this regard is very wide and it is expected of the Central Government to take cognizance of the conduct of the official liquidators in the proformance of their duties and obligations under the law, and also otherwise as Central Government servants. Thus, in the eye of the law, they are officers of the Government entrusted with liquidation work subject to such orders in regard to the processing in individual cases as might be passed by the Court.

13.6. The normal work of the official liquidator in settling the lists of creditors and the lists of contributories and taking effective steps expeditiously to take into possession all the assets of a company which has been wound up and to realise them, so that the funds available may be equally distributed amongst the creditors, etc., are of a highly technical nature. All these processes are time-consuming and the need for adequate staff is keenly felt in all the official liquidator's offices.

If the Central Government is to guide Official Liquidators effectively in future and if it is considered to be a matter of sufficient economic and social importance that winding-up proceedings must be expedited, it is necessary to strengthen the staff now attached to the offices of the Official Liquidators and to improve their quality.

13.7. The persons employed in the offices of official liquidadators should possess necessary legal and accounting qualifications and experience, particularly for the performance of the following types of work—

(a) investigation into the affairs of the company requiring the scrutiny of books of account, registers, minutes books and other books and papers and the preparation of reports for misfeasance proceedings;

(b) scrutiny of books and accounts for the issue of notices to creditors and debtors;

(c) scrutiny of the statement of affairs for preparing reports;

(d) verification of claims;

(e) field jobs like taking possession of assets, attending to sales thereof and ascertaining the position of the assets of debtors.

13.8. These varied types of work cannot be dealt with effectively and expeditiously with the present staff strength in

the offices of Official Liquidators. Since under the provisions of section 451 of the Companies Act, 1956, and under the Companies (Court) Rules, 1959, fees and commissions are paid to the Central Government out of the assets realised in liquidation, administrative expenditure involved in the staffing of the official liquidators offices is not a burden on the revenues of the Government.

13.9. Another important item of work was entrusted to the Official Liquidator by the recent amendments to section 497 and section 509 of the Act relating to voluntary liquidations. These sections now require the preparation of a report by the Official Liquidator for submission to the Court stating that the affairs of a company voluntarily wound-up have not been conducted in a manner prejudicial to the interest of its members or to public interest. This examination has to be taken up by the Official Liquidator after the voluntary liquidator completes his work and submits his final accounts. The amendments followed the findings in the report of the Vivian Bose Inquiry Commission and of the subsequent report of the Daphtary-Sastri Committee, which commented on the absence of any effective control over the activities of a Voluntary liquidator. While we recognise this criticism, we do not think that the organisation and machinery available in the Official Liquidator's offices are in a position to cope with this work. Apart from taking up the scrutiny of companies in voluntary liquidation, the Act provides for a scrutiny by the official liquidator of the affairs of a company to be transferred under a compromise or a scheme of arrangement placed before the Court under section 394 if such a company is to be dissolved without winding it up. The nature and magnitude of work involved is akin to an investigation into the affairs of a company. But such investigation in the case of liquidated companies involves scrutiny of records long after all the events took place; we do not think this is a fair burden to place on the Official Liquidators. In their testimony before us all of them complained of their inability to carry these onerous responsibilities and their views were supported by several witnesses from the professions, whom we examined.

We, therefore, recommended that the law on this subject be suitably amended to relieve the liquidators of this additional burden of work which they can hardly carry. In our view this important work of an investigational nature should be undertaken by the Department through its regional and state organisations only in the case of public companies including those public companies which have been converted into private companies.

13.10. Under the existing administrative arrangements the Regional Director is entrusted with the control

and supervision of all offices in a region—both the offices of the Registrars of Companies and the Official Liquidators. To assist him in the discharge of his duties vis-a-vis Official Liquidators, the Department of Company Affairs set up a year ago three Internal Audit Units, one each for the Eastern and Western regions and the third for the Southern and Northern regions combined. Each Unit consists of one Audit Officer, One Junior Technical Assistant and the necessary quota of lower staff. The Accounts Officer or the Senior Accounts Officer attached to the Regional Offices and the Department at Delhi guide the working of the internal audit team. The duties of the internal audit team are as follows:—

(i) to check vouchers and postings in cash books; central cash book;

(ii) to see that the books are written daily and correctly;

(iii) to see the registers prescribed under the rules are maintained up-to-date and written up in time;

(iv) to see that accounts, both under section 462 and section 551 of the Act, are prepared and submitted in time to the High Court and Registrars of Companies and audit objections are attended to and settled in time;

(v) to see that the assets are taken from companies in liquidation in time, they are entered in the books and properly looked after;

(vi) to see that the assets are disposed of expeditiously and that orders of the Government and the High Court are obeyed and that maximum price is secured and also that the cost of sale was not too high;

(vii) to see that expeditious action has been taken for recovery of book debts and suits are filed in time against debtors;

(viii) to examine the securities/share registers and the fixed deposits register and to see that the deposits are being properly administered, renewed in time and that cash in hand is not in excess of needs;

(ix) to see that all rents due on the property are received in time and accounted for.

13.11 We consider this administrative arrangement to be salutary, but would suggest that the Audit Officer for each region should be a person of sufficient rank and standing to be able to discuss matters on an equal

footing with the Official Liquidators. We trust the Official Liquidators would also look upon the Audit Officers as their colleagues engaged in a common task, and not as outsiders imposed on them. We also suggest and not as outsiders imposed on them. We also suggest that instead of one unit for the Southern and Northern regions combined, separate units for each of the region be provided in the interest of administrative efficiency.

II

13.12. In view of the delays inherent in the normal Court procedures, it has been suggested to us that the Central Government should assume increased administrative powers to help in the expeditious disposal of liquidation cases.

13.13. Section 555(7) (a) (b) of the Companies Act, 1956, has provided for dual and coequal jurisdiction both by the Central Government and the Court in the matters of payment of undistributed assets or return of capital to the creditors/contributories out of the 'Companies Liquidation Account'. Similar provisions can be made in respect of some of the other powers also. A party who is aggrieved by an order of the Central Government can always apply to the Court for a final determination of the matter, and, therefore, transferring of some of the powers of the Court to the Central Government will not in any way affect the parties adversely.

13.14. To give concreteness to our suggestions we append to this chapter a list of administrative powers in respect of liquidation proceedidngs which are now exercised by the High Courts, *in chamber*, and which we think could, without much damage to the basic principles underlying these provisions be transferred to the Central Government.

13.15. A large field will still remain open to the Courts under the existing provisions of the Companies Act relating to the winding-up of companies.

In conformity with our recommendation in the next chapter of our report regarding the appropriate from or organisation for the proper adjudication of company cases and judicial review of such cases where necessary, we would recommend that all other powers relating to the winding-up of companies should be exercised by the Company Tribunals which we propose should be set up in the principal administrative regions of this country.

As these Tribunals will be composed not merely of legal experts but also of others with the requisite knowledge of

company accounts, company finance and company management, we feel sure that the Tribunals willl be in a much better position than the traditional courts of law to deal expeditiously with the complicated legal, economic and financial issues involved in the liquidation and dissolution of a corporate entity.

13.16. In course of their evidence before us, the official liquidators brought to our notice the difficulties which they now encounter in dealing with winding-up cases because of difficulty in complying with several existing provisions of the Act. We have refrained from going into this matter because it would need changes in the law and the time at our disposal did not permit us to go into the question of the amendment of the Companies Act. The amendment of the provisions relating to winding-up proceedings, in particular, must, in our view, be preceded by a detailed examination of several sections of Part VII of the Companies Act. This task can be taken in hand only when Government decide to undertake a comprehensive major amendment of the Companies Act at an appropriate time. In this connection it has come to our notice that there are large number of habitually defaulting companies which fail to carry out the obligations under the Companies Act in spite of repeated reminders and prosecutions by the R.O.Cs. We consider it a very unhealthy state of affairs and as such we suggest that Section 433 of the Act may be suitably amended and the Registrars of Companies may be given power for winding up such companies.

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ANNEXURE TO CHAPTER XIII

An illustrative list of administrative powers under the winding-up provisions of the Companies Act, 1956, which would could be trasferred to the Administration

Serial No.	Section of the Act and Rules	Nature of duty/sanction	Reasons for the proposal
1	Section 454(3) read with Rule 128(2)	Extension of time by further period beyond three months	The period of 21 days fixed under Section 454(3) of the Companies Act is too short and no director will be able to submit the statement of affairs within the period. Usually courts extend the time. The Official Liquid tor is also anxious to get the statement of affairs filed. Court's time need not be wasted.
2	Section 454(4) read with Rule 129(2)	Payment of reasonable expenses to the person making the statement of affairs	It is purely an administrative matter between the Official Liquidator and the director/officer etc. Court's time need not be wasted. The Central Government can take over.
3	Section 454(4) read with Rule 129(3)	Expenses which are disallowed by the Official Liquidator	Same grounds/reason as above.
4	Section 457(1)(2) read with Rule 139(1)	General powers of the Official liquidator are those he can exercise with the sanction of the court	After the Official Liquidator has once obtained the leave of the Court for exercise of his powers under section 457(1) (2) of the Companies Act, and other matters need not to go to Court. He can apply to the Central Government for sanction
5	Section 464(3)	Composition of the Committee of Inspection	Under the 1956 Act it is now not necessary to app oint a committee of Inspection. There will be very few cases in which it would be necessary for such appointment.

Serial No.	Section of the Act and Rules	Nature of duty/sanction	Reasons for the proposal
6	Section 465(9) Proviso read with Rule 142	Not filling up of vacancy caused in the Committee of Inspection by the Official Liquidator.	Purely an administrative matter. Court's time need not be wasted.
7	Rule 146	Payment to the members of the Committee of Inspection	Purely administrative matter. Court's time need not to be wasted.
8	Section 512(2)	Exercise of powers by the Voluntary Liquidator subject to control of the Court	All references may be made to the Central Government since voluntary winding uprarely has to go to court.
9	Section 515 ..	Removal of the vouluntary Liquidator and appointment of persons as Liquidator other than O.L.	Powers can be transferred to the Central Government since a voluntary winding up has to go to the Official Liquidator finally for a certificate under section 497(b) and 509(b) of the Companies Act, 1956.
10	Sec. 546(1)(2)(3)	Certain powers of the Liquidator to be exercised subject to the sanction of the Court	Since the Supreme Court as not made any rule under section 546(1A) the Central Government may take over these powers.
11	Section 553(2)	Retaining money by Liquidator in excess of Rs 500/- for more than 10 days	Purely administrative matter. Court need not be troubled.
12	Rule 273 ..	Sale by the Official Liquidator	Can be covered by Section 457 of Companies Act.

Serial No.	Section of the Act and Rules	Nature of duty/sanction	Reason for the proposal
13	Sec. 557 read with Rule 203 Costs of meeting etc.	Application by Creditor of contributory for calling a meeting by the Liquidator.	This rule applies only to meeting s called by member. Voluntary winding up can be given to the Central Government.
14	Rule 280	Payment of dividend without proof if the amount is less than Rs 500/-.	Purely administrative matter.
15	Rule 308	Employment of additional staff	Purely administrative matter.
16	Rule 309	Apportionment of common expenses	Purely administrative matter.
17	Rule 321(2)	Resignation of Liquidator	Purely administrative matter.
18	Rule 338(1)	Costs and expenses payable out of assets in a winding up by the Court.	Purely administrative matter

CHAPTER XIV

Organisation for adjudication of company cases and judicial review of administrative action.

I

In two major directions in the area of supervision and control over company management, our Companies Acts, 1956, even when it was enacted, went considerably beyond the corresponding provisions of the English Companies Act. In the first instance, a much larger role was assigned to the executive government both in respect of the normal management of companies and of those internal problems not infrequently created by the arbitrary exercise of majority power by their Boards. Secondly, our new Act also conferred on the courts of law, and particularly on the High Courts, much wider powers than were vested in them by the similar provisions of the English Companies Act, 1948. We have commented on the powers of the executive government in some major areas of company management in some of the preceding chapters. In this chapter we shall consider the role of the courts of law, and especially of the High Courts, in the supervision of company affairs.

14.2. Judicial control over companies in our Act is based on the same philosophy as underlines the corresponding provisions of the English Companies Act and the pattern of such control is broadly similar to that of the English Act. For several generations past, our jurists and law-makers in this country followed the British tradition of regarding Company Law, in its substantive provisions, as largely an extension of the Law of Contract (and its constituents, Partnership and Trust) to the legal entity, known as the joint-stock company, as they viewed this institution. Most of the substantive provisions of Company Law were thus concerned to be an elaboration of contractual rights and fiduciary duties, while the procedural provisions of Company Law were intended to ensure that these rights and duties were acquired and performed according to the terms of fair contract as jurists then regarded them. It was a natural corollary of this basic thinking on the nature of Company Law that several matters covered by it were considered to be fit subjects for adjudication by the traditional courts of law and particularly by the established High Courts. Thus to start with, even the power of incorporating companies had been vested in the then Supreme Courts of

Bengal, Madras and Bombay. The Office of Registrar of Joint Stock Companies was established much later.

14.3 Broadly speakng, the supervisory powers given to the courts under the present law could be summarised under the following heads:—

(i) control on the admendment of Memorandum of Association and domicile;

(ii) control over reduction of share capital;

(iii) exercise of control over meetings of companies;

(iv) control over fraudulent directors and the recording of finding as to the desirability or otherwise of persons to handle corporate matters;

(v) control over the management and conduct of companies including the new power conferred on the courts by the Act of 1956, for the first time, to intervene in company affairs when they were carried on in a manner oppressive to minorities of shareholders or in a manner which was prejudicial to the interest of the company or which *prima facie* indicated gross mismanagement such as might jeopardise their solvency in the future;

(vi) supervision and control over the winding-up of companies;

(vii) control on compromises, arrangements, merges and amalgamations;

(viii) granting of relief in appropriate cases to managerial personnel from the consequence of negligence or breach of trust or defaults in complying with the provisions of the Act.

14.4. Section 10 of the Companies Act, 1956, conferred exclusive jurisdiction on the High Courts to deal with civil proceedings initiated or filed under its provisions. Subsection (2) of this Section however, enabled the Central Government to empower any District Court to exercise some of the jurisdiction conferred upon the High Courts by the Act. It has been brought to our notice that a notification under this provision has been issued in May, 1959 transferring to the District Courts some of the jurisdiction conferred by the Act upon the High Courts. As regards contravention of the penal provisions of the Act or of the provisions of the Indian Penal

Code or of other statutes which created offences, the jurisdiction to try such offences lies in the ordinary criminal courts, i.e., the courts of the magistrates and sessions judges, and the procedure laid down in the Criminal Procedure Code applies to them.

14.5. The net effect of all these provisions is that in regard to all civil proceedings, i.e., all proceedings other than offences triable in the criminal courts, the competent court to deal with company matters is the appropriate High Court, except in regard to those matters which have been transferred to the District Courts under Sub-Section (2) of Section 10 of the Companies Act. It was the substantive provisions of the Companies Act, 1956, which for the first time embodied in our Company Law several far reaching provisions with a large economic and social content involving not only complicated issues of law as in the past but also of economic and social policy, accounting and investment.

14.6. Adequate adjudication of such complicated issues as indicated above calls for some minimum basic knowledge of these subjects and some general familiarity with company structures, practices and management methods and techniques. In the old days, before the Act of 1956 came into force, when company organisation and practice was relatively simple and Company Law was essentially procedural, no high-degree of expertise or specialism was needed for the disposal of civil proceedings arising out of the Companies Acts, because judicial decision could be usually based on the application of the more familiar basic civil laws relating to contracts, trusts, transfer of property, sale of goods, master and servant, law of agancy, etc. When, however, problems of economic and social policy implicit in the concept of the public interest or the national interest were written directly or indirectly into the provisions of the Companies Act and a new concept of the interest of companies as distinct from the interest of the share-holders and creditors was given explicit recognition in some provisions of the Act, Company Law ceased to be merely a law for the adjudication of conflicting contractual rights and obligations as between the parties which collaborated in the formation of a company. In large areas of company practice, the more fundamental issue was the extent to which the private interest of the concerned parties could be reconciled with the public interest implicit in the aims and objects of our acepted economic and social policies. In this wider context, the spectrum of the edjudication process necessarily calls for the inclusion within its range an adequate comprehension not mearly of the rights and obligations of the parties in the contractual sense but also of the concepts of sound company practice, efficient economic management of companies, the social obligations of business, and in some respects the good of

the community which the companies serve. This exercise involves in practice much more than an evaluation of evidence, oral or documentary, with which the traditional courts of law in all countries which boast of a reasonably sound judicial system have been mostly concerned in the past.

14.7. This type of judgment calls for a more complex appraisal, valuation and assessment of company methods and practices which are usually outside the normal training experience and background of lawyers and judges brought up on the British common law traditions and on the methods and procedures of the traditional courts of law. The conventional wisdom of practitioners in the law offices and law courts was apt to concern itself primarily with matters related to legal technicalities which are essentially within the sphere of the traditional common law. By contrast the sphere of policy laws (or what is often called 'political laws' although not in a prejorative sense) deals with problems of economic and social change in an area which is far from certain and constantly shifting in the light of social and economic developments. These laws are concerned essentially with the respective rights and powers of public authority in relation to individuals or groups in the state. To this field belong the right of business and of labour to organise, concentrate and monopolise, social security legislation of all kinds, matters of education and training, etc., all of which have such a general impact on the life of the community that they call, sooner or later, for legislative, administrative; and in some cases; judicial action. It is because of the fact that the issues arising out of these matters are at present so much outside the ambit of the conventional wisdom of the traditional judicial establishments in several countries that, in these fields, most modern states have inincreasingly resorted to specialised administrative tribunals for adjudication of these issues. Unless there is a substantial change in the education, training and experience of lawyers from among whom judges are mostly recruited—any such change can be expected to come about only in the long run and as a result of deliberate educational policy— it would remain mostly a matter of accident if some of them, through Government service or service in public companies, acquire some special knowledge and experience of what is known as the 'administrative process' in dealing with issues in the broad field of 'policy laws'. It is against this backgraund that the well-known Committee on Administrative Tribunals in the United Kingdom, presided over by Lord Oliver Frank observed some time ago that the "reflection on the general social and economic changes of recent decades convinces us that tribunals as a system. of adjudication has come to stay..... We agree with Donoughmore Committee (1932) that the tribunals have certain characteristics which often give them

advantages over the courts. These are cheapness, accessibility, freedom from the technicalities, expeditious and expert knowledge of their particular subjects." In this connection it may be pertinent to quote the following observations of Lord Greene, then Master of Rolls in the United Kingdom, on advantages of certain classes of cases being dealt with by Tribunals to the exclusion of ordinary courts:—

> "In deciding whether a case falls within these classes it is relevant to consider the number of individuals likely to be affected and their probable pecuniary position; the necessity or otherwise of providing a speedy and inexpensive procedure, and one affording opportunity for decentralisation; whether the questions likely to arise are predominantly questions of fact and whether expert knowledge and experience are desirable for their decision and the extent to which the jurisdiction is to be based on discretion rather than on fixed rules and precedents."

Judged by these principles it is absolutely clear that the problem arising out of the administration of the Companies Act, are essentially those which could properly be comprehended and analysed only by persons well versed in Company Law, Accounts, Management and practice.

14.8. Several official witnesses who appeared before us as well as others drew attention to the delays and inadequacies of the traditional courts of law in handling many company cases. We do not wish to refer to any instances to illustrate our argument.

We are, however, convinced that it is most desirable that administrative tribunals should be set up at least in the more important commercial centres of this country, and that an appellate administrative tribunal with some limited original jurisdiction might with advantage be set up at the seat of the Central Government to handle and dispose of the increasingly large number of company cases which are now referred to the courts of law. The jurisdiction of these administrative tribunals might also include adjudication of cases falling under other Acts which are directly or indirectly concerned with the working of the corporate sector,

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14.9. If our recommendation on this subject is accepted, Government will have to consider the following problems re-

lating to the organisation and administration of these tribunals:—

(i) the structure of the administrative tribunals of original jurisdiction and of the appellate administrative tribunals;
(ii) the duties and responsibilities to be allotted to these tribunals ;
(iii) the relationship of these tribunals with the High Courts and in particular with the Supreme Court;
(iv) the rules of procedure to be followed by these tribunals, which must necessarily be substantially different from the time consuming procedure in the traditional courts of law;
(v) the composition of these tribunals, which must be manned by specialised personnel including lawyers, accountants, investment experts, management specialists and administrators, with the requisite training and experience and would need to be directed by the best qualified among the members of the tribunal, and not necessarily always by those who have served as judges in the High Courts;
(vi) the methods of recruitment to these tribunals, which should differ materially from the existing methods of recruitment of judges.

14.10. We have refrained from going into the details of these practical administrative issues which will need to be thrashed out before the system of administrative tribunal which we have recommended can be installed. We would, however, like to dissipate two common misunderstandings about administrative tribunals which have hitherto prejudiced the case for them in this country. Since our judicial system was based on the common law system of England many of us in this country inherited an understandable bias against institutions which, in their views, seemed to affact the so-called unity of the common law system. This argument has never unduly disturbed lawyers, jurists or judges in any country in the European Continent. We do not see why a system of administrative tribunals such as we envisage cannot be fitted into the structure of our judicial administration without in any way adversely affecting the prestige or the authority of the higher courts in the country. The other argument about public confidence in the traditional courts of law is also linked with our past history and experience. We are justifiably proud of our higher courts of law, but in any rational view of the relevant issues, it is necessary to remember the fact that such confidence as our people have in the existing higher courts of law stems essentially from the fact that no other judicial system was known to us till lately.and not because of the intrinsic superiority of the existing system over the alternative parallel

system existing in the European Continental countries, provided the system of administrative tribunals is organised, structured and manned by personnel of the requisite education, training and experience, and their procedures are so designed and worked out as to cut out needless formalities and delays, we are confident that the management of companies, the shareholders and creditors and workers and all those who are connected with the working of the corporate sector will develop an equal measure of confidence in the new courts of law that we envisage. The rapidity with which a multitude of administrative tribunals have sprung up even in countries where the judicial system is squarely based on the Common law system as in England provides support for our view that the growing complexities of modern business call for a different type of judicial approach from what can be reasonably expected from the traditional courts of law. It is necessary for the Administration and Government to face this reality, and to devise a system of adjudication of cases under the Companies Act and other related statutes which alone can ensure adequate fulfilment of the economic and social purposes underlying them.

14.11. In making our recommendation on the subject, we have not overlooked the fact that a Companies Tribunal, in some respects resembling a body that we envisage, was set up by Government on July 1, 1964 with its headquarters at New Delhi, under the Companies (Amendment) Act, 1963. Under Section 10A of the Companies Act since repealed by the Companies (Amendment) Act of 1967, the powers conferred on the Companies Tribunal were limited to those which were hitherto exercised by the ordinary courts of law under the following Sections and appeal against refusal to register transfer of shares exercised by the central Government under Section 111.

Section 155	...	Power of the Court to rectify register of members.
Section 203	...	Power to restrain fraudulent persons from managing companies.
Section 234A	...	Seizure of documents by Registrar.
Section 240	...	Production documents and evidence.
Section 240A	...	Seizure of documents by inspector.
Section 388B	...	Reference to Tribunal of cases against managerial personnel.
Section 397	...	Application to court for relief in cases of oppression.
Section 398	...	Application to court for relief in cases of mismanagement.
Section 403	...	Interim order by court.
Section 635B	...	Protection of employees during investigation by Inspector or pendency of proceedings before Tribunal in certain cases.

14.12. The Tribunal was empowered to set up Benches consisting of not less than two members to be appointed in such manner as Section 10B of the Act prescribed. The usual power of a court of law under the Civil Procedure Code was conferred on the Tribunal which was deemed to be a Civil Court for the purposes of Section 195 and Chapter XXV of the Code of Civil Procedure, and proceeding before which were also deemed to be judicial proceedings. Provision for an appeal against the decision of the Tribunal or its Benches were made to the High Court having jurisdiction over the piace at which the Registered Office of the company concerned was situated; but such appeal was to be lodged only on questions of law except in regard to the findings of the Tribunal under Section 388D of the Act relating to the continuing employment of the managerial personnel referred to under this Section.

14.13 This Tribunal was, however, abolished by the Companies (Amendment) Act 1967 for the reasons mentioned in the Statements of Aims and Objects appended to this Bill and also explained more fully by the Minister of Industrial Development and Company Affairs in course of the debates Parliament. As far as we can make out, the main reasons for this decision were:—

(i) the relatively small volume of work done by the Tribunal during a period of three years;

(ii) the somewhat time-consuming procedure adopted by the Tribunal, which had the effect of defeating the main purpose for which it was established, namely, the expeditious disposal of company cases;

(iii) the centralisation of the work of the Tribunal virtually at Delhi apart from its periodical visits to Bombay, which caused avoidable hardships to parties;

(iv) the very limited jurisdiction conferred on the Tribunal, which seemed to be concerned only with powers under Sections 397, 398 of the Act and one case under Section 388B of the Act.

It is possible that another reason for the disappointment expressed by the administrative authorities at the highest level at the outcome of the Tribunal's work was the approach adopted by the Tribunal to the cases presented to it. This was hardly distinguishable from the procedure adopted by the judges sitting on the High Court Benches. In a sense, this was perhaps inevitable both because the Chairman who presided over the Tribunal was a former High Court Judge and the training, experience and competence of the Members of Tribunal did not include close or sustained

familiarity with the problems of trade and industry or with the organisation and working of joint stock enterprises with which they had to deal.

14.14. We do not wish to pursue further the circumstance in which the ill-fated first experiment with an administrative tribunal in the field of company administration came to such an abruptend—except to say that, from the records available to us, we have been unable to find out the reasons why more serious thought could not be given to the appropriate constitution of the Tribunal; why the jurisdiction of the Tribunal was limited to a relatively small number of Sections of the Companies Act; why the work of the Tribunal had to be centralised in Delhi causing needless inconvenience to the parties concerned, why the Administration did not take adequate steps immediately after the coming into force of the Companies (Amendment) Act, 1963 to frame appropriate Rules for the Tribunal providing for a summary procedure and a summary method of hearing; and lastly why it was left to the Tribunal to frame its own elaborate regulations based on the traditional procedures under the Civil Procedures Code and the High Court Rules, when one of the primary objects behind the decision to establish the Tribunal was to get away from the usual delays inherent in such procedures.

14.15. In the light of our thinking on the subject and the evidence that we received from many quarters, we are clear in our mind that the reasons for the failure of the first Companies Tribunal to realise the expectations of its sponsors do not in themselves rule out the case for the setting up of a properly constituted administrative Tribunal with Branches situated at the various Regions to which the powers of the court conferred under the various Section of the Companies Act could be transferred for final disposal, with a provision for appeal to an Appellate Administrative Tribunal at Delhi on questions of fact and law, and in special cases, a further appeal to the Supreme Court only on questions of law. We need hardly repeat and emphasize the fact that only a highly selective membership of the Tribunal reflecting the type of varied competence needed for dealing with complicated business issues, aided by a carefully worked-out summary procedure could be expected to ensure the successful working of any Tribunal. Unless these conditions are fulfilled, we see little possibility of any such Tribunal producing the results expected of it.

14.16. In the proposals which we have made for the establishment of an Administrative Tribunal, a suggestion has been made to reduce the current delays in the disposal of company cases by transferring to a Tribunal and to another similar Appellate body the jurisdiction now conferred on the

High Courts to deal with problems arising out of the administration of the Companies Act. In this context we are conscious of the powers conferred on the High Courts under Articles 226 and 227 of the Constitution of India.

> But we trust that our suggestion for an in-built alternative remedy by way of appeal to an Appellate Administrative Tribunal at the Centre, and for a further appeal on questions of law to the Supreme Court of India will be found to be in accordance with the accepted cannons of limitation on the exercise of the prerogative writ jurisdiction and the High Courts will not be called upon to interfere in company cases in exercise of their extraordinary powers.

We have thought fit to give expression to this view in the light of decisions in certain cases which have come to our notice, in respect of which more than one High Court have taken cognisance of the same matter, thereby frustrating the progress of the cases for a number of years.

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CHAPTER XV

Miscellaneous Provisions

In the foregoing chapters of this report, we have dealt with those major problems of the administration of the Companies Act which in our judgment have a close bearing on its enforcement and implementation. If our recommendations are accepted, we have no doubt that, collectively, they would greatly add to the quality of the administration and enhance its efficiency and effectiveness. In the process the aims and objects underlying the Act would also be much better and more meaningfully realized.

Lacunae in the Act—Simplication of reports & returns.

15.2 We have not been able to deal with several other matters which were brought to out notice by witnesses. For one thing, in the view which we took of our terms of reference, they were crowded out of the mainstream of our deliberations by more prior issues. In any case, within the limits of time at our disposal, it would not have been possible for us to deal with all of them, and in respect of some of the other issues we have suggested that they should be the subject of further detailed study to be undertaken by the Department of Company Affairs or the future Administration, whatever its shape may be. Under this latter head fall two major issues, namely—

(a) the question of filling up several important lacunae in the Companies Act, 1956; and

(b) the question of the simplication of the reports and returns which are required to be submitted under the provisions of this Act.

We have referred to these two matters already in chapter IV of our report, and trust that our suggestions would be followed up with appropriate action by Government without much delay.

Government Companies

15.3 We have also refrained from dealing with the application of the Companies Act to Government companies, i.e. , companies in which the Central Government or the State Governments singly or jointly hold more than 50% of the equity shares.

While it is clear that several provisions of the Companies Act cannot be usefully applied to Government companies as defined under the Act, our general view is that the Act should apply to Government companies in the same way as it applies to the non-government companies; otherwise, the already existing incipient feeling in business circles that there is undue discrimination in favour of Government companies will further grow.

Some criticism was also voiced before us by several witnesses that, while the provisions of the Companies Act are applied very stringently to companies in the private sector, those in the public sector are allowed to carry on their business untrammelled. If the management of Government companies or the administrative departments dealing with them consider that certain specific provisions of the Companies Act should not apply to them, it should be for them to make out a case for exemption of such Government companies from these provisions. Section 620 of the Companies Act enables the Central Government to modify the Act in relation to government companies in the manner indicated in that Section. One of the requirements of this Section is that copies of the necessary notifications exempting government companies from the provisions of the Act must have the approval of the two Houses of Parliament. We think this is a salutary requirement and government companies should have no difficulty in complying with this procedure.

15.4. In this context we should like to mention a point made to us by a few witnesses.

We were told that neither in the formative nor in the operatvie stages of government companies did the administrative departments concerned or the management of such companies maintain as close contact as they might be expected to have with the Department in charge of the administration of the Companies Act. If our recommendation about the need for close coordination of work between the Bureau of Public Enterprises and the Department of Company Affairs is accepted, this, we hope, will ensure much closer coordination between government companies and the Department concerned with the administration of the Companies Act.

Need for laying down target dates for disposal of cases.

15.5. Another important point made by some witnesses to ensure quick disposal of cases was that suitable target dates should be fixed for this purpose. We understand that shortly

after the establishment of the then Department of Company Law Administration, a detailed time schedule was laid down for the processing of cases under different heads and for their final disposal within the time limits set in the schedules. We were also told that sectional heads, the Under-Secretaries and the Deputy Secretaries in charge of the Branches were required to look into all cases where limits were not being observed and to bring them to the notice of the other senior officers of the Department including the Secretary. We hope that this practice is being followed, as we consider it a very laudable administrative practice.

In this connection we recommend that—

(a) these time schedules for particular classes of cases should be widely made known to the business community ;

(b) the Under-Secretaries and Deputy Secretaries concerned should keep close watch on the observance of the target dates prescribed ;

(c) in all cases of appreciable deviation from the targets, they should be brought to the notice of the Joint Secretaries and the Secretary of the Department depending on their importance ;

(d) suitable administrative action on undue delays in the disposal of cases should be taken against the officers and staff concerned; and lastly

(e) in the Annual Report on the Administration and Working of the Companies Act for the previous year, a list of cases where there has been a substantial deviation from the target dates fixed for them should be conveniently reproduced.

Some urgent accounting reforms.

15.6. Several useful recommendations were made to us by some professional witnesses about the accounting methods and procedures. We consider the following suggestions to be deserving of particular notice:—

(a) It was suggested that a uniform accounting year should be prescribed for all companies.

It was realised that this would be a significant break from current practice and companies might require a reasonably long notice to switch over to a uniform year of account. This suggestion has been considered off and on for more than a decade now, and we consider that the time has now come when the

companies should be required to fall in line with it from such suitable future date as Government may prescribe. If it helps to overcome conservatism and intertia.

> **We suggest that a beginning towards this very desirable and may be made by requiring at least all companies falling under the same industrial classification to conform to one uniform accounting year.**

In the second stage of progress the same accounting year for all companies could be fixed from a convenient future date. We do not see that there are any special difficulties in conforming to this change. On the contrary, it would be of advantage alike to the private sector and to Government to be able to study and analyse comparable data for different companies within the same industrial classification, and this would be possible only if common accounting years are provided or them. We suggest this this proposal should be discussed at a high level with the industrial and commercial associations and a suitable date, may be two years from now, should be fixed by which time all companies would be required to comply with the new requirements;

(b) Secondly, it was suggested to us by shareholders' associations and by several spokesmen of the stock exchanges that public companies listed on the exchanges that public companies listed on the exchanges should be required to publish at least half-yearly reports on their work and accounts, if not quarterly.

This should be a healthy development in the corporate sector and we have little doubt that it will help to encourage investments in company shares and debentures.

> **If necessary, we would recommend a simplified version of the accounts to be made available along with the half-yearly reports leaving the details to be provided along with the annual reports as at present.**

Here again, preliminary discussion with the accountnacy profession would be needed, and we have no doubt that they would be able to evolve suitable forms of summary accounts which could be easily filled-up by the companies concerned without any appreciable burden on their professional and secretarial staff;

(c) Thirdly, one important reform connected with company accounts which has been a subject of much discussion in the past not only in this country but also abroad and which was again taken up with us by some witnesses concerns the accounts of composite companies, i.e., companies whose principal

business is not confined to one or two allied lines of manufacture or trade but covers activities which fall under several industries or trades. We do not wish to enter into the theoretical arguments for or against these 'diversified' companies as they are sometimes called. But we make two specific recommendations which cut across the arguments on this subject.

(i) We consider it essential that all 'diversified' public companies should be required to prepare separate accounts for the different lines of business carried on by them, so that the performance of the different units in such companies may be known and made available on request, to shareholders and to Registrars of Joint Stock Companies.

We do not consider that there could be any serious objection to this type of disclosure. In practice most progressive companies at present prepare such accounts for the internal use of their management. So the technical difficulties which are sometimes urged against the preparation of such accounts cannot be considered to be insuperable. Our proposal only ensures that these accounts may be available to such shareholders who may reasonably ask for them and to Government;

(ii) We consider that it is very desirable that the Directors' Reports for 'diversified' companies should invariably include brief accounts of the performance of the different units in such companies so that their actual performance and their problems and difficulties, if any, may be made known to their shareholders.

In this connection we would invite attention to the provisions of Section 17 of the English Companies Act, 1967, which requires the Directors of 'diversified' companies to include in their Report a statement of—

(1) the proportions in which the total turn-over of the company during the accounting period is divided among the turn-over in respect of the different units; and

(2) as regards the business of each unit, the approximate expenditure in monetary terms, to which in the opinion of the directors the carrying on of the business of each of these units contributed to, or restricted, the profit or loss of the company for that year before taxation.

(d) As regards the accounts of group companies, we recommend that a consolidated statement of the accounts

of all companies within a group should be prepared. Such companies should not thereafter be required to attach the accounts of its subsidiaries along with its own accounts. It would, however, be open to any shareholder of the holding company to ask for the accounts of any or of all the subsidiary companies and it should be the duty of the holding company to make these documents available to such shareholder.

Foreign Companies

15.7. A point of some interest relating to foreign companies as defined in Section 591 of the Companies Act was brought to our notice by the Controller of Capital Issues. At present hardly any control is exercised over the registration of such companies. They are free to establish any place of business in India and to carry on their business as they like, as long as they do not engage in any industrial enterprise that requires a licence under the Industries (Development and Regulation) Act. The Companies Act does not apply to such companies except in respect of the matters mentioned in Sections 592 to 606.

We, therefore, accept the suggestion of the Controller of Capital Issues that the Reserve Bank should not specifically issue a permit to any foreign company to establish a place of business before any such company is registered in this country. We also recommend that the adequacy of the provisions of the Companies Act, 1956, in Part XI should be examined afresh in order to consider how more affective supervision could be exercised over the activities of foreign companies operating in India.

In this context, it has been brought to notice that many foreign companies working in India are foreign only to the extent of their place of incorporation; their entire business operations are carried on in India. In those cases there is nothing in the Companies Act, 1956, which would ensure that the business of these companies is carried on in comformity with the basic principles underlying our Company Law. On this basis a question was posed before us as to whether it was justifiable that while foreign companies, which were deemed to be so only because of their place of incorporation were allowed to operate freely without any control, indigenous companies should be handicapped by the obligation imposed on them to conform to the requirements of our law. It was also argued that while several provisions in the Act attempted to safeguard public interest *vis-a-vis* the working of indigenous companies, no such attempt was made in the case of foreign companies operating in India. The provisions of the Act in respect of enquiry, investigation, inspection and

special audit were also not applicable to foreign companies working in India.

In our view, therefore, these issues relating to foreign companies of this type need to be re-examined urgently against the background of our general economic policy relating to the role of foreign business and investments in this country.

15.8. We have refrained from considering several aspects of our contemporary economic policy relating to the role of foreign business and foreign investments although some witnesses brought them up before us. As a Working Group on Company Law and Company Administration, we took the view that this was a subject primarily for the Study Team on Economic Administration presided over by Shri C. H. Bhabha. We hope that recommendations of this Study Team would in due course be considered in the light of their impact on the working of collaboration agreements in joint ventures. Nevertheless, we should like to take this opportunity of emphasising the importance and urgency of reviewing our present policies regarding the terms and conditions of foreign participation in Indian enterprises. In particular, having regard to the necessity, increasingly brought home to us in recent months by the exigencies of our current and foreseeable foreign exchange budgetary position, for an objective balancing of the benefits and costs of foreign participation in joint ventures, we feel that an important object of our future policy in this area should be to safeguard the position and powers of the Indian partners in joint ventures and to ensure that their status and authority as the 'management on the spot' are not undermined. Even where the foreign participant is a minority holder in the equity of an Indian company, it has come to our notice that no effective control is at present exercised to prevent the acquisition of increasing control over the management of the company by the foreigner through market operations, resulting in an increase in the share of the equity held by him. Neither the Companies Act, 1956 nor any other law on this subject can at present impose any effective check on the slow and unobtrusive transfer of management control in such cases. Our policy in this regard needs to be sharply defined, and fair and legitimate conditions, capable of easy enforcement, should be laid down at the time of approval of the collaboration agreements by Government. We have in this context noted the provisions of section 250 of the Companies Act, 1956, but we feel that an investigation contemplated in that section was not designed for the type of problem which has been to our notice.

We understand that the Department of Industrial Development is now engaged in a review of the present

policy of Government relating to foreign investments in the light of the existing pronouncements by authority on this subject. We trust that as soon as this examination is concluded, the Department of Company Affairs and the Department of Industrial Development should jointly consider the problem posed before us and take such suitable steps as may be necessary to ensure that the Indian character of management in joint ventures is not merely maintained but also strengthened; and in the case of companies where the Indian character of companies has been prejudicially affected as a result of transfers of shares not duly approved by the management of these companies, Government should arm itself with the authority to review such cases in order to restore the original position regarding the shareholding of such companies. For this purpose, it may be necessary to incorporate suitable provisions in the Companies Act, 1956, in the analogy of the provisions of section 409 of the Act, which was, of course, intended for a different purpose. We do not wish to go further into the possible legislative safeguards that might be necessary, but would recommend that this basic aspect of foreign collaboration arrangements is taken up for consideration by the Departments concerned as soon as Government have re-defined their policy towards foreign investments in joint ventures.

15.9. Several shareholders' associations claimed before us that it was time that government 'recognised' them as they had recognised the stock exchanges. In reply to our queries the representatives of these Association informed us that the main reason for asking for this recognition was that in its absence they enjoyed no status *vis-a-vis* the management of companies. It was difficult for them to approach the latter and often their requests for information about the working of companies were turned down or remained unheeded.

We are in sympathy with this demand and consider that Government should initiate a system of recognition, after consultation with the leading shareholders' associations in Calcutta, Madras and Bombay.

The only practical difficulty that we visualise might arise from the fact that in some geographical areas there might be more than one shareholders' association at work. In such cases some principles would have to be laid down for discriminating among these associations and selecting one of them for recognition. We do not think that it would be difficult to draw up suitable criteria for this purpose.

Spurious Share Certificates

15.10. It is a statutory duty of every limited liability company to issue share certificates in the prescribed form and manner. The nature, numbering and the validity of share certificates, as well as their transfers and transmissions are governed by the statute and the rules framed under it. Sections 82 to 90 and 108 to 113 of the Companies Act, 1956 together with the Companies (Issue of Share Certificate) Rules 1960 at present regulate these matters. Prior to the coming into force of these statutory provisions and Rules, the law was not sufficiently clear, and in any case, was found inadequate to prevent the issue of spurious share certificates.

15.11. While the changes in the Companies Act and the rules framed under it in 1960 have imposed some wholesome restraints on the recklessness of unscrupulous company operators, they have not been able to root out the possibility of such adventures. This is clear from some recent disclosures in Parliament and elsewhere. The circulation of spurious shares has its origin in two sources. Firstly, though the manipulation of persons connected with the management of companies or with their connivance and secondly through outside operators. The first type of fraudulent dealings in duplicate share certificates was noticed on a large scale a few years ago in several companies in the Mundhra Group. It is unnecessary to go into the *modus operandi* followed in these cases. It will suffice to mention that in order to ensure that the fraud might not be detected, the Managing Agents and the Directors of the company secreted or destroyed the share registers. The second type of fraudulent dealings concerns cases where the requisite signatures etc. are forged on the duplicate share certificates. Such certificates may or may not be issued with the connivance of the management.

15.12. In cases arising out of the issue of spurious shares the rights and liabilities of the holders of shares whether they are registered as members of the company concerned or not; of its management, and of the companies themselves are somewhat involved, except in clear cases of fraudulent dealings where the signatures on the duplicate shares are forged, involve difficult problems of conflicting legal claims. We do not propose to enter into any detailed disquisition on this subject.

In view of the few cases of alleged issue of forged shares whiich have come to our notice, we would, however, strongly urge that suitable provisions should be made in the Companies Act to facilitate quick adjudication of these conflicting claims, so that the interests of the companies do not suffer and they may not needlessly

become involved in prolonged litigation resulting in liabilities which may financially cripple them.

15.13. In this connection the details of the case of Messrs. Rishardson Cruddas and Co., Ltd., a company in the Mundhra Group were reported to us by the official witnesses. A former Solicitor to the Government of India before Independence had been appointed as long as 1957 as a Special Official to deal with the problems which arose from the issue of a large number of forged shares in this company, apparently with the knowledge and connivance of its the then management. Yet, no substantial progress towards the settlement of the outstanding issues had been made even after the lapse of 10 years, and we were told that numerous suits were still pending in the Calcutta High Court. We understood that they related not only to the adjudication of claims *inter-se* as between those who claimed title to the shares as members but also to claim for damages against the company itself for alleged losses sustained by those whose claims had not been accepted by the Special Officer of the Government of India.

15.14. Incidentally, this Officer expired about a year ago.

It is clear to us that some summary procedures for dealing which such tangledwebs of claims and counter-claims in cases of this type must be devised within the framework of our company law. We, therefore, recommend that Section 155 of the Companies Act, 1956 should be suitably amended and elaborated to enable an appropriate authority to settle such disputes finally. If our recommendation for the establishment of a Tribunal for dealing with company cases is accepted, a matter of this type must necessarily be refferred to this body.

In this connection, we should like to comment on a view which was expressed by a spokesman of the Department of Company Affairs who appeared before us. We are told that it might be difficult to amend section 155 adequately; some legal experts had opined that any consideration of the claims of holders of allegedly spurious shares might *imply* a partial recognition of the existence of such shareholders, and this would be opposed to the basic contractual principles which govern the relations between the members of a company and the company itself. We do not wish to get involved in the subleties of this legal logic, but we hope that this argument should not cramp the style of the Department of Company Affairs and hinder its initiative. In any case, we are clear in our mind that no aspect of this problem can directly or indirectly affect the right of a court of law or a duly constituted Tribunal to go into its merits. The scope of section 155 of the Companies Act is, in our view, sufficiently wide to permit adjudication on the relative claims of the so-called genuine and the allegedly spurious shareholders, in a case where the genuineness of the shareholders itself is involved.

15.15. So far as the prevention of fraudulent dealings in duplicate shares is concerned, the existing provisions of the Act, if effectively enforced should go far to prevent such duplication. Section 84 of the Companies Act, 1956, was amended in 1960 by the addition to it of sub-sections (ii), (iii) and (iv). These new sub-sections provide *inter alia* for the circumstances in which certificates can be renewed or duplicates can be issued.

The detailed procedure to be followed by the company management for the issue of share certificates has also been laid down in the Companies (Issue of Share Certificates) Rules, 1960 which provide reasonable safeguards against the issue of spurious duplicate shares. Nevertheless there is need for adjudication of the conflicting claims in those cases where disputes arise as to the authenticity of share-scrips. For this latter purpose, some special amendment of the provisions of the Companies Act is needed. For the reasons which we have already mentioned, we do not think any special legislation is necessary, as we consider that the scope of section 155 of the Companies Act is wide enough to offer sufficient jurisdiction to a court of law or to a Company Tribunal to adjudicate on the type of issue of conflicting rights and claims which we have discussed.

15.16. In this connection a suggestion was made to us that in the interest of companies as well as of the commercial banks, it might be desirable to provide for safeguards against pledge of the same scrips with more than one bank issued with the connivance of the company management.

We recommend that the Reserve Bank of India should examine the feasibility of requiring scheduled banks which advance loans exceeding say, Rupees five lakhs to any one borrower against shares, to furnish the essential Particulars of the scrips pledged with them to the Reserve Bank of India.

(Sd.) D. L. MAZUMDAR,
Chairman.

(Sd.) KALI MUKHERJEE,
Member.

(Sd.) H. P. NANDA,
Member.

(Sd.) R. K. HAZARI,
Member.

(Sd.) P. B. MENON,
Member.

(Sd.) M. V. VENKATARAMAN,
Member.

(Sd.) S. VENKATARAMAN,
Member-Secretary.

ANNEXURE A

LIST OF PERSONS/ASSOCIATIONS WHO SUBMITTED WRITTEN MEMORANDA BEFORE THE WORKING GROUP ON COMPANY LAW

1. Shri C. C. Chokshi, Mafatlal House, Bombay.
2. Shri N. C. Krishnan, Chartered Accountant, Madras.
3. Shri S. M. B. Eswaran, President, Madras Share-holders Association, Madras.
4. Shri T. K. Sivasamban, Madurai-1.
5. Shri K. Venkataraman, President, Madras Stock Exchange.
6. Shri D. C. Kothari, Madras.
7. Shri A. Ramaiya, Madras.
8. Shri A. K. Sivaramakrishnan, Chartered Accountant, Madras.
9. Shri B. K. Ramadhyani, Bangnalore.
10. Shri P. Brahmayya, Chartered Accountant, Madras.
11. Shri N. Krishnan, Managing Director, International Instruments (P) Ltd., Bangalore.
12. Shri B. L. Sethi, Retd. General Manager, Bank of Rajasthan, Jaipur.
13. M/s. Peirce Leslie & Co., Cochin.
14. Shri R. Venkatesan, Chartered Accountant, Fraser & Sons, Madras.
15. Shri V. D. Kapadia, Bombay.
16. Shri G. K. Devarajulu, Coimbatore.
17. Shri S. K. Bagla, Chairman, Calcutta Stock Exchange, Calcutta.
18. Shri T. S. Santhanam, Madras.
19. Associated Chambers of Commerce & Industry, Calcutta.
20. Shri C. C. Desai, M. P., New Delhi.
21. The Federation of Indian Chambers of Commerce and Industry.
22. The Northern India Share-holders Association.
23. Shri Chamanlal C. Shah, Solicitor, Bombay.
24. Chartered Institute of Secretaries, Calcutta.
25. Shri M. C. Bhandari, Chartered Accountant, Calcutta.

26. The Institute of Chartered Accountants of India, New Delhi.
27. Shri K. B. Labke.
28. Sir James Lindsay, Metal Box Co., Ltd., Calcutta.
29. Society of Incorporated Secretaries of the Corporation of Secretaries, London, Calcutta—Shri M. A. Hamid.
30. Bharat Chambers of Commerce, Calcutta.
31. Shri Bhaskar Mittar, Calcutta.
32. Bombay Shareholders Association.
33. Shri A. R. Shervani, Allahabad.
34. Shri P. L. Tandon, Hindustan Lever Ltd., Bombay.
35. Shri B. P. Khaitan, Solicitor, Calcutta.
36. Shri K. N. Mookerjee, Calcutta.
37. Shri C. H. Bhabba, Bombay.
38. Shri Harbans Singh Mehta, Delhi Stock Exchange Association, Ltd.
39. Shri S. C. Roy, Calcutta.
40. Shri K. J. George, Director (FIC), Ministry of Industrial Development and Company Affairs, New Delhi.
41. Shri N. C. Maitra, Department of Economic Affairs, New Delhi.
42. Shri K. Vaitheeswaran, Official Liquidator, Madras.
43. Shri T. J. Gondhalekar, Regional Director, Company Law Board, Madras.
44. Shri M. V. Warekar, Regional Director, Bombay.
45. Shri S. M. Yausuf, Registrar of Companies, Bombay.
46. Shri A. V. Ekambaram, Dy. Director (Inspection), Madras.
47. Shri H. K. Ganguli, Official Liquidator, Calcutta.
48. Shri M. K. Venkatachalam, Director, Investments Department of Economic Affairs, New Delhi.
49. Shri K. S. Sundara Rajan, Minister (Economic), Embassy of India, U.S.A.
50. Shri J. P. Mukherji, Registrar of Companies, West Bengal, Calcutta.
51. Shri V. D. Sonde, Stock Exchange Division, Bombay.
52. Shri B. J. Rele, Official Liquidator, Bombay.
53. Shri T. S. Kannan, Financial Adviser, Richardson and Cruddas, Bombay.
54. Shri M. R. Bhide, Chairman, Life Insurance Corporation Bombay.
55. Shri R. S. Bhatt, Chairman, Unit Trust of India.

ANNEXURE B

LIST OF PERSONS INTERVIEWED BY THE WORKING GROUP ON COMPANY LAW ADMINISTRATION

Bombay : from 5th to 7th October, 1967.

1. Shri M. P. Bhide, Chairman, LIC.
2. Shri S. G. Bhave, Secretary, Industries Department Government of Maharshtra.
3. Shri R. S. Bhatt, Chairman, Unit Trust of India.
4. Shri H. B. Hari Bhakti, President, Institute of Chartered Accounts of India.
5. Shri C. C. Shah, Solicitor, Bombay.
6. Shri A. Bakshi, Deputy Governor, Reserve Bank of India
7. Shri P. L. Tandon, Chairman, Hindustan Lever Ltd.
8. Shri T. J. Jeejee-bhoy, President, Bombay Stock Exchange.
9. Shri V. D. Sonde, Director, Stock Exchange Division, Department of Economic Affairs.
10. Shri Tanubhai D. Desai, President, Bombay Shareholders Association.
11. Shri M. V. Warekar, Regional Director, Company Law Administration, Bombay.
12. Shri S. M. Yausuf, Registrar of Companies, Maharashtra
13. Shri B. J. Rele, Official Liquidator, Bombay.

Madras : from 27th to 30th November, 1967

1. Shri N. C. Krishnan, Chartered Accountant Madras
2. Shri S. Narayanaswamy, Chitra & Co., Madras.
3. Shri V. K. Devarajulu, Laxmi Mill Co., Coimbatore.
4. Shri B. K. Ramadhyani, Chartered Acountant,, Madras
5. Shri P. Brahamayya, Chartered Accountant.
6. Shri M. S. Sundararajan, Chartered Accountant.
7. Shri R. Venkatesan, Chartered Accountant.
8. Shri A. Ramayya, Advocate.
9. Shri S. M. Eswaran & others—the Madras Shareholders Association.
10. Shhri S. Mohan Kumaramangalam, Bar-at-law.

11. Shri T. S. Santhanam.
12. Shri A. K. Sivaramakrishna, Chartertd Accountant
13. Shri T. J. Condhalekar, Regional Director, Company Law Administration.
14. Shri A. V. Ekambaram, Deputy Director of Inspection, Company Law Administration.
15. Shri K. Venkataraman and Shri Krishnamurthy of Madras Stock Exchange, Ltd.
16. Shri K. G. Kuruvilla.
17. Shri K. Vaitheswaran, Official Liquidator, Madras

Calcutta : from 19th to 22nd January, 1968.

1. Shri M. C. Bhandari.
2. Shri B. P. Khaitan.
3. Shri A. L. Goenka.
4. Associated Chambers of Commerce—Represented by Mr. D. Fordwood and others.
5. Shri S. K. Bagla, Chairman, Calcutta Stock Exchange.
6. Chartered Institute of Secretaries, India Association. Rep. by S/Shri R. N. Sen Gupta, P. J. Ricketts, L. R. Puri, S. K. Basu.
7. Shri P. M. Narielvala, Chartered Accountant.
8. Association of Company Secretaries and Executives Rep. by Sarvshri B. S. Kothari and R. Saraogi.
9. Bharat Chambers of Commerce—Shri L. R. Das Gupta and others.
10. Shri A. M. Byne, Representing Central Government Solicitors and Shri Bessani.
11. Shri Bhaskar Mittar.
12. Shri H. K. Ganguli, Official Liquidator, Calcutta.
13. Shri S. V. Ayyar, President, Institute of Cost and Works Accountants.
14. Shri J. P. Mukherjee, Registrar of Companies, Calcutta.
15. Sir James Lindsay.
16. Shri M. A. Hamid, Society of Incorporated Secretaries.
17. Shri K. P. Bhargava, Chartered Accountant.
18. Merchant Chambers of Commerce.

Delhi : from 15th to 17th Febfuary, 1968.

1. Shri S. K. Datta, Chairman, Company Law Board.
2. Institute of Chartered Accountants—Sarvshri Hari Bhakti and Balakrishnan.

3. Shri R. M. Bhandari, Financial Adviser, Bureau of Public Enterprises.
4. Shri C. H. Bhabha.
5. Federation of Indian Chambers of Commerce and Industry—Sarvshri G. L. Bansal, Dr. Bharatram and others.
6. Shri S. Bhoothalingam.
7. Shri T. S. Kannan, Richardson & Crudas.
8. Shri N. Subramanian, Special Secretary, Ministry of Industrial Development, and Shri R. V. Subramaniam, Joint Secretary, Ministry of Industrial Development.
9. Northern India Shareholders Association—Rep. by Shri Jaitly and others.
10. Shri M. K. Venkatachalam, Director, Investments, Department of Economic Affairs.
11. Shri N. Dandekar, M.P.
12. Delhi Stock Exchange—Rep. by Shri Harbans Singh Mehta and others.

सत्यमेव जयते

CHAPTER XVI

Findings and Recommendations.

Chapter II

1. The efficient management of companies is a matter of concern not only to the shareholders and other interests connected with their workig but also to the national economy and the public interest.(2.24)

Chapter III

There are some essential pre-conditions to the purposeful and effective administration of the Companies Act and related matters. These are - (a) first, that the policies embodied in the provisions of the Act should be spelt out with sufficient concreteness, so that there may be no difficulty in translating them into operational terms; (b) secondly, there should be a reasonable measure of commitment to these policies, alike on the part of ministers and other policy makers connected with their Administration and of the senior civil servants entrusted with the responsibility for their implementation; (c) thirdly, the relevant statutory provisions should be reasonably free from ambiguity; and (d) fourthly, the executive rules, regulations and instructions framed under the statute, with due regard to good company practice, should be clearly worded and internally consistent. (3.6)

Chapter IV

There have been frequent amendments of the Companies Act in the past; it may not be unfair to infer that they were conceived and designed primarily to deal with ad hoc issues, with arose from time to time and which could not obviously have been based on any total view of company law and its bearing on the working of joint stock companies. (4.2).

2. A comprehensive look at the detailed provisions of the Companies Act and also of the other related statutes, some of which are at present administered by other ministeries and departments, should be undertaken at an appropriate time as soon as the legislature has dealt with the Monopolies and Restrictive Trade Practices Bill which, we understand, is now before a Select Committee of Parliament.(4.2)

3. The object of this overall review which we suggest would be to undertake a detailed study of the specific provisions of the Act in relation to the other related Acts with a view to -

(a) coordinating and integrating the policy decisions embodied in these provisions and now administered by different departments in an un-coordinated and fragmentary manner; and

(b) assessing the total burden imposed on the Administration in order to find out how much of it could be reduced through changes in the technical requirements of the law and better coordination and integration of the administration of other statutes now administrated by other ministries and departments. (4.2)

4. We, recommend the setting up of a competent expert Committee to have a detailed scrutiny of the various returns, bearing in mind the purpose for which they were originally conceived, and at the same time taking into account the actual use that is made of these returns in the offices of the Registrars. (4.3)

Chapter V

1. We recommend that the present definition of a private company contained in the Companies Act, 1956, should be amended and a private company properly so called should be defined as a company which

(i) restricts the right to transfer shares;

(ii) limits the number of its members to 50 excluding employees;

(iii) prohibits any invitation to the public to subscribe for any shares in or any debentures of the company; and

(iv) restricts its borrowings from the public and from financial institutions, other than banks, set up under statutes or under the authority of the Central or State Governments on from any other public company, not being a banking company, to 50 per cent of its paid up capital. (5.5)

2. We suggest that the Department may scrutinise the list of the returns which private companies are required to file as well as many of the formal provisions of the Act applicable to them with a view to limiting the requirements of the law applicable to them to a minimum. (5.6).

Chapter VI

1. We consider it very important that the law relating to the organisation, structure and the powers and duties of management of companies should be such as would enable management

to discharge their responsibilities. The pre-dominant form of management in the corporate sector of this country in terms of corporate assets was till lately represented by the Managing Agency System in terms of corporate taxes. With the rapidly declining importance of the system, it will be necessary to strengthen alternative forms of management through Boards and Managig Directors and to develop in the top managers capacities for initiation and promotion of enterprises. (6.2)

2. The economic and social requirements of modern business will need a forum where the Managers of the future could have them sorted out and integrated, in the overall interest of all the parties participating in an enterprise. We have considered whether it might not be advantageous to provide in our Indian Law for a modified pattern of the two tier system originally set up in Germany and since adopted in several countries of the European Community. A logical corollary of this type of set-up would be the institution of collegiate or plural executives rather than the familiar one-man executive as represented by the Managing Director of a typical Indian company.

In course of our enquiry we were told that many companies were already unobstrusively moving towards the type of management set up which distinguishes between the supervisory and the management functions. We do not, however, think that the time is yet ripe for writing into our company law any specific provisions on this subject. Instead we suggest that the developments in the wake of the abolition of the Managing Agency system should be carefully watched, and studied. Meanwhile, we suggest that, in their own interest, the business leaders should consider whether it would not be advantageous to encourage the growth of an informal type of collegiate management under the broad supervision and control of a composite board of directors. We have reason to believe that if senior executives of companies who have the power to take subordinate decisions could be given access to the management board, and could participate on an equal footing with the top management in major decision-making, the efficiency, quality and the harmony of management would considerably increase. (6.2, 6.4, 6.5).

3. We consider that an appropriate management structure for public companies should be provided by one or more full-time managing directors or whole-time working directors, or whole-time managers who must have seats on the Boards of these companies. Following the abolition of the Managing Agency System, we should like the law to provide compulsorily for at least one Managing Director or one wholetime Director, or a Manager with a seat on the Board of every public company.

The Companies Act, 1956 already provides that no one can be appointed to be a Managing Director for more than two public

companies except with the approval of the Central Government. We consider that this prohibition should also extend to private companies, i.e., no one who is a Managing Director of a public company shall be appointed Managing Directors of four companies in all including private companies. (6.6).

4. In the context of the re-organisation of the management structure of companies in future, we have also to consider the question of the participation of workers' representatives in the management of companies. Although a few witnesses raised this issue before us on the analogy of the provisions relating to workers' representation on the German Supervisory Boards, we felt that the time had not yet arrived for any such provision in our law. Nor did the demand for such representation on the Boards of companies appear to us to be particularly strong or insistent. (6.7)

5. We are inclined to take the view that it is only after further improvements have been made in workers' rights and more systematic and comprehensive use has been made of a wide range of joint determination within an enterprise in its day-to-day activities, that statutory representation of workers in the management of companies whether at the top (Board), middle (Executive management) or lower (Shop-floor) levels can be considered. (6.8)

6. Before any attempt is made to provide for the statutory representation of workers at any desired level in company management, efforts should be made to improve the education and training of workers for some of the elementary tasks of management. In the circumstances of this country, it would be idle to expect to obtain, in the near future, the right type of people for higher level of management than for the shop-floor level.

We do not consider that it is necessary at present to provide in the Companies Act compulsory representation of workers at any level of management. But it is our hope that it may be possible for the management of companies increasingly to associate with them workers' representatives, particularly at the shop-floor level, so that all management decisions that affect the interest of workers can be taken in the full light of the discussions with workers' representatives. (6.8).

7. We are not sure if the provisions of the law should also provide for compulsory representation of the consumers or of the general public on the Boards of companies. On the whole, we are inclined to the view that, unless further discussion and debate has clarified many of the issues relating to election or selection of representatives of consumers and the general public, it is not necessary to provide in the law for any such representation. (6.9).

8. While we are in sympathy with the claim that the minority of shareholders should be adequately protected through representative on the management of companies, we are somewhat hesitant about recommending a compulsory system of proportional representation for all or even selected groups of companies. Out hesitation arises from the fact that the present provisions of section 265 of the Act which give an option to a company to adopt proportional representation for the appointment of Directors has hardly been used even in these cases where several groups of shareholders constituted substantial minority. Nor are we quite sure if the complications involved in working out a system of proportional representation would not seriously prejudice the relations between the Directors representing different groups among shareholders and the company. Indeed the entire subject of proportional representation in the context of the provisions of that Section requires further detailed study. Government should initiate this study immediately, so that when Companies Act 1956 is comprehensively amended in future, a further close look may be given to the present virtually inoperative Section 265 of the Act. We should like Government to examine a specific suggestion made to us by some witnesses, viz., that where a substantial minority of shareholders ask for the appointment of a Director in addition to those who are already on the Board it should be necessary for a company to appoint him to the Board, notwithstanding, anything in the Articles of the company or the provisions of the Act relating to the election of Directors.(6.10)

9. We feel that the time has come when the right to speak should be extended to a proxy.(6.11)

10. We are of the view that the Companies Act should now provide compulsorily for the appointment of qualified secretaries in the case of all large public companies say, with a paid-up capital of Rs.50 lakhs or more. We also recommend that suitable qualifications for such Secretaries should be prescribed by Government. These should be such as will include persons who have passed the examination organised by Government on an All-India basis and obtained diplomas from Government, and other who have passed recognised academic or professional examinations directly concerned with the management of companies.(6.12)

Chapter VII

1. We feel that the Administration should be able to lay down, in general terms the type of individuals, who would prima facie be judged unfit for appointment as managing or whole-time directors of public companies, and to make its general policy known to the business community and to the shareholders and

others directly concerned with the management of companies. Section 274 of the Act says down some disqualifications of directors. We suggest that the Administration should consider the feasibility of adding to this list in the light of its administrative policy as regards the appoinment and re-appoinment of managing or whole-time directors. This will be in the nature of a supplementary list of disqualifications intended for the guidance of the business community, although deviations from these further conditions might be considered by the Administration in exceptional cases. (7.5)

2. Under Section 275 of the Companies Act, 1956, no person can be director of more than 20 companies. This number excludes private companies, unlimited companies, associations carrying on business for no profit, and all companies in which an individual is only an alttrnate director. Many witnesses who appeared before us considered that this number was unduly large and needed to be reduced to 10 in case of public companies and 15 in the aggregate inclusive of private and other companies, but exclusive of associations carrying on business for no profit. We agree with this view and suggest a suitable amendment of the Act in due course.(7.6)

3. In our view no one who has attained the age of seventy should be permitted to continue as a director, and no deviations from this rule should be permitted. (7.7).

4. We were told that many companies had on their Boards a few well-known names, knowing fully well that they could not devote time or thought to the policies or programmes of the companies. This we consider an undesirable practice. We, therefore, recommend that a suitable provision in the Companies Act should be made either to do away with this practice or at least to mitigate its evils by limiting the number of ordinary directorships which a managing or whole-time director of a public company can hold to not more than two or three. The fees received by such a director for attending the Board meetings of the other companies should, we consider, be surrendered on a suitable basis to the company or companies of which he may be a managing or whole-time director. (7.8).

5. We understand that Government have recently taken a tentative decision to prohibit contributions to political parties or for any political purpose. If this is so, we endorse this decision, although we recognise that contributions for this purpose could and perhaps would still be made deviously out of a company's funds, which may not be easy to detect from the company's published accounts. This is, however, no argument for the law to continue to countenance the present practice.

6. While we agree that suitable amendments of the existing laws should be made to prohibit contributions to political

parties or for political purpose out of company funds, we do not consider that similar curbs on the use of company funds for charitable purposes, which are duly recognised as such in the revenue or other laws of the country are called for except that such contributions should be disclosed in the company's published annual accounts. (7.8).

7. We understand that Government have already taken a decision as to the abolition of the managing agency system in the near future. We presume that the institution of Secretaries and Treasurers would for similar reasons, be also abolished at the same time. (7.14).

8. We consider that it will be more appropriate for the Administration to fix a suitable remuneration for the Chief Executive of a company after taking into consideration all relevant factors, in relation to its size and the nature of its business and the qualifications, experience and background of the selected Chief Executive and, of course with due regard to the company's profit-earning capacity for the entire period of his first appointment, and to treat this as the minimum remuneration admissible to him under section 198 of the Companies Act.

The provisions of this section permit this course to be followed in all these cases where a monthly payment is proposed to be made. As a safeguard, Government may reserve the right to call for regular periodical information about the performance of a company at any time, and indeed as often as it considers necessary to do so, during the period of the first appointment of the Chief Executive, in order to satisfy itself that the remuneration sanctioned for him is justified. (7.19).

9. Our broad conclusions on the question of control over managerial remuneration are as follows :—

(i) Within the limits of the statutory ceilings, prescribed for such remuneration in sections 198, 310, 326, etc., of the Companies Act, 1956 and subject to the maximum administrative ceiling laid down by Government, the shareholders should be free to fix the remuneration of the Chief Executive of a company at an appropriate level after taking into account all the relevant factors which are now considered by Government in fixing the remuneration payable to them. The decision of the shareholders should be taken by a special resolution at a meeting;

(ii) This decision should be conveyed to Government within a fortnight of the special meeting to be held for this purpose;

(iii) Government should have the right to call for such further information as they wish to have in regard to any such decision and to order any suitable modifications in the proposed remuneration or in the terms and conditions of employment of the Chief Executive of a company, within a period of two months of the receipt of the certified copy of the special resolution passed by the company. If no such information is called for or no objection raised within 60 days, the company's proposals would be deemed to have been approved;

(iv) In regard to minimum remuneration, Government should sanction a reasonable remuneration, in the case of salaried employees, for the entire period of the first appointment of a Chief Executive, in the case of a new company.

(v) In the case of going concerns, the remuneration duly approved by Government should be deemed to be the minimum remuneration for a period of two to three years at a time. If at the end of this period it is found that the amount of remuneration sanctioned is in excess of the statutory limit, Government should have the right to review the case and to prescribe such other remuneration as may be appropriate to the fortunes of the company. For this purpose suitable guiding principles should be framed and communicated to the Chambers of Commerce and other trade associations.

(vi) In order to give publicity to the decisions of the Company Law Board on the terms of remuneration approved for managerial personnel, the Board should take steps to publish approved terms in the suitably abridged form in its fortnightly journal where it is already publishing the appointments and re-appointmets of managerial personnel. (7.22).

10. We do not think that the criticism about the present procedure and practice followed by Government with regard to cases dealing with inter-corporate investments and loans are fully justified. On the contrary, we consider that the reasons which promoted the imposition of the present restrictions on inter-company investments still exist, and that, in the circumstances of company management in this country and in order to prevent dissipation of a company's resources and undue concentration of economic power in a few hands, it is necessary to maintain some curbs on the freedom of management to invest in the shares of other companies. In this connection our attention has been drawn to the need for encouraging investments

in priority industries. We have not doubt that in considering applications for inter-company investments in excess of the limits laid down in Section 372 of the Companies Act, the Administration will take due note of the desirability and importance of encouraging investments in such industries, provided the managements of the companies concerned can be depended upon to make good use of such investments, and the resources of the investing company permit of such investments without detriment to its own legitimate needs. (7.24)

11. We do not consider that the operation of the statute relating to inter-corporate investment has been unduly severe or that the powers conferred on the Central Government have been exercised with undue rigidity. We, further note that since the present provisions were inserted in the Companies Act, 1956, the guiding principles formulated by Government have taken due note of the legitimate needs and requirements of business.(7.25)

12. We do not think that the obligation cast on the public companies by the procedure laid down for examination of cases relating to inter-corporate investments is unduly onerous.(7.25)

13. We have considered a suggestion for doing away with the requirement of the Central Government's prior approval if investments in excess of the permissible limits are duly approved by the company at a special meeting. We do not consider that this suggestion would be of any advantage to the companies. On the contrary, it might well create problems and difficulties which the present requirement about prior approval of the Central Government avoids. (7.25).

14. In the case of inter-corporate loans we suggest that the criteria to be taken into account by the Administration in dealing with applications under section 370 of the Companies Act should include (i) the financial position of the applicant company; (ii) the financial position of the horrowing company; (iii) the security offered; (iv) the rate of interest on the loans; (v) the terms and conditions for the repayment of the loan ; (vi) the purpose for which the loan was proposed to be given; and (vii) the present position of the loan and investment portfolios of both the lending and the borrowing companies. (7.26).

15. In view of the liberal margin on which companies have the freedom to operate under the provisions of Sections 370 and 372 regarding inter-corporate investments and loans, we do not consider that there is room for any legitimate apprehension about the effects of these provisions on company practice or on the orderly growth and expansion of corporate business. (7.26).

16. With the progressive abolition of the managing agency system, there is good reason to think that many of the erstwhile managing agents would like to enter directly or indirectly into sole selling agency agreements with the companies which they managed previously. We, therefore, suggest that Government should consider the strengthening of the provision of section 394 of the Act, and particularly of sub-section (4)(b)(ii) of this section, so as to enable them to keep a close watch on the tendency to use the selling agency agreements as a device for unduly adding to the remuneration of the management of companies. (7.30).

17. A good deal of intensive home work will have to be done by the senior officers of the Department, in consultation with selected representatives of trade and industry and marketing experts, to evolve appropriate guide lines for the use of departmental officers entrusted with the responsibility for the administration of the provisions of the law relating to sole selling agents. The object of these guidelines would be (a) first, to work out the norms and yard sticks with reference to which selling agency agreements would have to be examined, and (b) to prescribe standard terms and conditions subject to which such agreements could be entered into. (7.31).

18. If an effective administrative machinery could be built up for examining cases of sole selling agencies, and only subject to this condition we would recommend that having regard to the importance of this matter, copies of all sole selling agency agreements entered into by public companies with a turn-over, over a prescribed limit in any particular line of trade or industry, should be submitted to Government for registration in the regional offices. It should be open to Government to modify the terms of these agreements at any time during their pendency after hearing the parties concerned, and companies should be required to give effect to these modifications with effect from such date as Government might indicate. (7.32).

19. We were told that one likely bye-product of the proposed abolition of the managing agency system would be the appointment of relations and friends of managing directors or directors or of the firms and companies in which such directors were directly or indirectly interested as sole selling agents of the companies concerned. This development would need to be carefully watched. We would recommend that if this tendency grows rapidly, the law should be suitably amended to require that in such cases, the terms and conditions on which selling agency agreements were to be entered into should be approved by a special resolution of the companies concerned, within a period of six months for these agreements, and that the commissions or other payments proposed to be made to the selling agents in such cases should suitably be isolated in the profit and loss accounts of companies. (7.33).

20. It is important to ensure that spurious organisations calling themselves by such names as Consultants, Technical Advisers, Agents or Special Officers, are not used as a device for channelling the profits of companies into the hands of the erstwhile managing agents or their associates. As a rule, we consider that the best way of remunerating genuine Consultants or Technical Advisers would be to compensate them by means of fees so calculated as to ensure that the payments are commensurate with the value of their services and not by means of *ad hoc* percentage of commission on gross profits. Anyhow, these practices to which our attention has been drawn need to be closely watched by the Department of Company Affairs. In particular we suggest that where a percentage of gross profits is proposed as remuneration for such organisations, it should be subject to ratification by the company in general meeting within a period of not more than six months from the date of their appointment. Government in the appropriate Ministry may also consider a system of registration of Consultants, Technical Advisers, etc., who should be called upon to conform to certain essential minimum conditions before they are permitted to offer their services to be business community. (7.34).

Chapter VIII

1. Recent thinking in the advanced western countries of the world has been concerned with the problem of devising an appropriate internal forum, within a company's structure itself, where a reasonable balance of power between the management of a company, its shareholders and its employees can be struck. In the absence of any such institutional forum, our Indian thinking during the last decade has been concerned with the problem of providing external controls largely through the machinery of the Administration. We feel sure that it will be generally agreed that, to the extent that an appropriate institutional structure is built up within the organisational frame of a company which provides a forum where the management of a company, its shareholders and its employees can participate in major decision-making, the need for external control over companies will correspondingly diminish. Till then, however, the working of companies and those responsible for their management need to be placed under the discipline of a reasonable measure of statutory regulation and control. (8.5).

2. Section 265 of the Companies Act 1956, permits a company, if it so chooses, to adopt the method of proportional representation for the election of representative of shareholders on its Board. In practice, however, little use has been made of the powers already given to companies under this section. (8.6).

3. A great majority of Company managers in this country consider that it is better to have a cohesive Board working on

the basis of straight majority voting, rather than one containing conflicting groups or factions. Also the demand for proportional representation by the shareholders themselves or the shareholders' associations has been very limited. In these circumstances we do not consider that any amendment in the law is called for at present. We have already stated in para 6.10 that the subject should be studied further. (8.6).

4. We feel that much more concentrated thinking on the subject of minority representation on the Board need to be done by the active minority shareholders any by shareholders' associations in different parts of the country, before they can legitimately seek the aid of legislation to support their moves. (8.7)

5. Unless Section 408 is radically overhauled so as to empower Government directors to intervene more effectively in decision-making by a majority in important matters, we do not think that it is likely to achieve the objects for which it was intended. We, therefore, suggest that Government should consider how this section could be suitably amended. One way of investing Government directors with effective powers would be to empower them to hold up decisions in respect of some specified areas of company management and to refer them to Government if they were of the view that such decisions would be oppressive to any members of the company or might prejudice the interest of company or might be against the public interest, if they were given effect to by the Board of the company. (8.9)

6. It seems to us that if the powers vested in the courts under sections 397 and 398 of the Companies Act are to be effectively utilised some far-reaching changes in the structure of the judicial machinery as well as in the procedures and in the rules of business of the relevant judicial institutions would be essential. (8.10).

7. Although a view was expressed in our Group that the removal of the requirement under section 397 and 398 (under those sections the right to apply to a court of law can be exercised only by not less than one hundred members of a company or by not less than 1/10th of the total number of its members, whichever is less) might lead to the abuse of the processes of law, we feel that if one or more individuals desired to apply to a court of law to have his or their grievances thrashed out, it would not be proper to deny them access to the courts and that if the courts felt that the processes of law were being abused it would be possible for them to take appropriate action when the applications were considered by them. (8.10)

8. We recommend as already mentioned in para 6.11 that the least than can be done to enable shareholders who are in a position to do so to express their views at company meetings is to confer on the proxies the right to speak at company meetings. (8.11).

9. We feel that there may be some advantages in changing the Auditors of companies at least every five years. We recommend that this proposal should be examined by Government in consultation with the Institute of Chartered Accountants before any change in the existing law is made. (8.12).

10. A good deal of detailed study will have to be undertaken into the principles and contents of both 'efficiency and social audit' before appropriate procedures and techniques in respect of such audits can be evolved. Till then it is hardly possible for any Companies Act to require that the accounts of public companies or at any rate, of some of them, should be subject to such audits. We do not, therefore, consider it practicable at this stage of the development of the accounting profession in this country to provide compulsorily for such audits in our Companies Act in respect of public companies, whether in the private or the public sector. (8.13).

11. It is necessary for us to emphasise that the problems involved in the installation of any system of 'efficiency' audit and, to a much greater extent, of 'social audit' are not so much organisational or administrative but essentially technical. Neither among the company auditors dealing with the accounts of companies in the private sector nor among the official auditors belonging to the offices of the Comptroller and Auditor-General or the Director of Commercial Audit, we have at present many persons who have either sufficient acquaintance with the principles of such audit or who are familiar with the methods and techniques which have to be used in these types of audit. Till the profession of accountancy in this country has built up a cadre of such highly specialised auditors, it would be futile to emulate the example of other countries and to try to duplicate institutions which have been set up elsewhere. (8.14).

12. We strongly urge that Government should do all that they can to help the Institute of Chartered Accountants and the sister Institute of Cost and Works Accountants to develop their technical and research sides. They should be encouraged to undertake high grade study and research into the principles of 'efficiency and social' auditing, and into the methods and techniques appropriate to such special audits. Simultaneously, the Institutes should be suitably assisted, so that they can secure access to the best available knowledge on this subject in some of the western countries, and may be able through a system of exchange of personnel to built up a cadre of well-trained specialists within its ranks. It is only then that thoughts about

'efficiency' and 'social' audit can become a reality in company audit in this country instead of remaining, as they now mostly seem to do, merely heavily loaded phrases which only embody vaguely articulated hopes and intentions. (8.15).

Chapter IX

1. We consider that the original objective underlying the present procedure as well as the organisational set up for implementing the provisions of section 209(4)(b) of the Act for evaluating the level of efficiency of companies was not very realistic, however, laudable in theory it might have been. It can, however, be a useful instrument for finding out materials and facts which could justify initiation of investigating inspections and 'special audits'. (9.10).

2. We feel that it is essential to integrate the work of inspection officers at the regional levels with the field organisation of the Regional Directors and Registrars. This would mean in practice that the officers attached to the Inspection Wing in the regional offices should work wholly under the administrative control of Regional Directors and should form part of the set-up of regional offices. This will facilitate their working in close concert with the Registrars of joint stock companies who are already under the control and supervision of the Regional Directors. The Director of Inspection and his staff at the headquarters of Department at Delhi should be concerned primarily with the formulation of principles of inspection and its methods and techniques and provide technical guidance, where needed, to the Regional Directors and the regional inspection staff. There will still remain a good deal of detailed home work to be done at the headquarters of the Department in evolving appropriate principles of inspection for the guidance of the departmental staff and for working out an integrated procedure relating to the implementation of sections 234(b), 235, 237 and also section 233A dealing with the special audit of companies. The powers conferred on the Administration under these various sections are at present exercised on a somewhat *ad hoc* and haphazard basis, and no unifying principles or integrated procedure for appropriate action under those different sections appear to have been so far evolved. This is a task on which, we suggest, the Director of Inspection at the headquarters of the Administration with the nucleus of staff stationed there should concentrate. Our proposals for the reorganisation of the work of inspection are, therefore, as follows :—

(1) the Central Director of Inspection should be concerned with the formulation of the principles of inspection and the methods and procedure to be followed by the inspecting officers and their staff

after periodical consultations with the Regional Directors;

(2) he should also be entrusted with the duty of working out similar principles and procedure for initiating action under section 234(4) and section 233(A) of the Act relating to the special audit of companies;

(3) he should further offer, whenever necessary, technical guidance in individual cases to the Regional Directors and the regional inspection staff, and in all cases of inter-regional inspection where a carefully concerted strategy of inspection will have to be devised for the officers and staff of different regions to ensure effective co-ordination of work among them;

(4) the administrative responsibility for the day-to-day supervision and control over the work of the inspecting staff should vest in the Regional Directors;

(5) the reports of the inspecting staff should be finalised in consultation with the Regional Directors, and in cases of inter-regional inspections, after consultation with the Central Director of Inspection ;

(6) on the basis of inspection reports the Regional Directors should take such follow-up action as may be needed in all matters in respect of which powers have been delegated to them under the Act. (9.10).

3. We suggest that the work and organisation of scrutiny cells should be reviewed at a very early date, and steps should be taken to cut out all infructuous exercises and to concentrate on selective, meaningful scrutiny of annual accounts and other routine company returns that are now submitted to the Registrars of companies. At the same time advantage should be taken of our proposals for the reorganisation of the work of inspection to strengthen the 'scrutiny cells' in the offices of Regi trars of companies with personnel of a higher calibre and quality. This may be done by replacement of some of the existing clerical staff by qualified technical people.

4. We suggest that in future, inspections under section 209 should ordinarily be the first preliminary step to an investigation under section 235 or 237 of the Act. (9.13).

5. With regard to the special audit of companies under section 233A, we regret to observe that this power has been hardly used by the Administration, although this section was incorporated in the Companies Act as early as 1960. (9.14).

6. In order to ensure more effective action, we consider it essential to create a combined office of Director of Inspection, Investigation and Prosecution at the Centre. (9.15).

7. The proposed office of the Central Director of Inspection, Investigation and Prosecution should be manned with persons possessing expert legal and accounting knowledge, training and experience. (9.15).

8. The proposed office of the Director of Inspection, Investigation and Prosecution should have broadly three divisions, (a) one, dealing with policy matters. i.e., the formulation of principles and procedures, including methods and techniques for inspection, investigation and prosecution of company cases ; (b) an executive division dealing with inter-regional or all-India investigations, and (c) a second executive division dealing with the prosecutions arising out of such investigations. (9.16).

9. Advantage should be taken of the proposed re-organisation of the present Directorate of Inspection in the manner indicated above to bring into this Directorate those Secretariat branches which are at present concerned with inspection, investigation and prosecution, so that unnecessary duplication of work between the Directorate and the Secretariat branches may be avoided. The details of the set-up will no doubt be examined by the Department of Company Affairs. We, however, suggest that it may facilitate decision-making and the implementation of decisions if the senior officers of the Directorate, as proposed to be reorganised, are given appropriate secretariat status. (9.17)

10. The Regional Directors or the Registrars should not be relieved of their work relating to the investigation and prosecution of relatively small cases of local importance. They will continue to be responsible for the handling of such cases, but here as in the case of inspections, they will be entitled to call upon the technical help and guidance of the new office in all important cases or even in regard to other cases where they feel that such help is needed by them (9.18).

11. Section 388B confers on the Central Government the power to refer cases against managerial personnel to a court of law. If our recommendation relating to the formation of a Companies Tribunal is accepted, we suggest that all such cases should be referred to that Tribunal.

It is clear to us that, in order that effective use can be made of this section, it is necessary for the Administration to formulate clear-cut objectives and policies on this matter, to see that summary procedure has been evolved for dealing with such cases, and that a properly constituted Tribunal manned by qualified

and experienced persons with adequate knowledge and understanding of company methods and practices who are in a position to pronounce with authority on issues of business ethics and morality has been set up. (9.19).

12. We suggest that in cases of employees who might be called to give evidence in petitions under section 397 and 398, the period of protection given under section 635 of the Act should be limited to a period of five years from the date of the conclusion of the proceedings before a Court of Law or Tribunal or the submission of the report by the Inspector whichever may be later. We agree that this limitation on a company's power to punish its employees cannot be construed as an unreasonable restriction as it merely subjects the company's action to a review by the Central Government. Further, it will be open to a judicial authority, i.e. the appropriate High Court or a Tribunal to review Government's objection on an appeal to it. This will, we hope, ensure that the interests of management are not unduly affected (9.21).

Chapter X

1. We feel that there is still need for a good deal of mere intensive home work in the Department of Company Affairs on the guiding principles relating to some of the discretionary powers vested in the Administration. (10.4).

2. We consider that these guiding principles should be disseminated among the members of the business community as widely as possible. (10.4).

3. We suggest that the following steps may be taken in regard to these guiding principles :

(i) the representatives of the interests likely to be affected by the use of discretionary powers should be informally consulted before the guiding principles are finally drawn up by the Department ;

(ii) these principles should thereupon be brought to the notice of all recognised Chambers of Commerce and Trade Associations including the Trade Unions and Consumers Associations where they exist.

(iii) adequate publicity through the departmental publications, the Press and by other means should be given to these guiding principles;

(iv) the Regional Directors and Registrars of Companies in the different States should explain these guiding

principles at formal or informal meetings to all those who may be affected by them in the leading centres of trade and industry within their jurisdiction. (10.4).

4. We consider it very important that the Annual Reports submitted to the Parliament from year to year should be debated fully, within the limits of time available for this purpose, having regard to the exigencies of Parliamentary business. Parliamentary vigilance in such matters should be reasonably effective and not merely symbolic. Likewise, the Chambers of Commerce and trade associations should also make a special point to study, examine and consider the guiding principles which the Administration may have laid down from time to time, instead of merely confining themselves to generalities of economic philosophy or economic policy. For this purpose they would need to organise their work properly, and must be served by personnel of the requisite education, training and competence. (10.5).

5. We are of the view that if the administration of the Companies Act cannot be entrusted to a high power statutory authority or commission of the type envisaged by the Bhabha Committee, the least that Government should do would be to endow the present Advisory Committee set up under Section 410 of the Companies Act, 1956, with powers and responsibilities in respect of those areas where the Administration now exercise wide discretionary authority in regard to many aspects of company management and practice. (10.8).

6. All members of the Working Group agree that Government should seek the advice of the Advisory Committee before the formulation of general principles and guide lines regarding the exercise of the Central Government's discretionary authority in respect of the powers conferred on them under the provisions of the Act, but opinion was divided as to whether such advice should be sought for the exercise of the discretion in regard to individual cases, as was done as long as the old Advisory Commission set up under the Act of 1956 was in existence. The majority of the members thought it was not necessary to obtain the advice of the Advisory Committee in deciding on these individual cases, but the Chairman of the Group and Shri Kali Mukherjee felt that it would be a valuable safeguard to all concerned to revert to the old practice. (10.8).

7. All members of the Working Group were agreed in emphasising the need for giving adequate publicity to the recommendation of the Commission, whatever they might be. Further they also felt that reasons should be given for the decision taken by the Commission or Committee on particular cases and where such decisions departed from earlier decisions, the justification for such deviation should be properly explained. (10.8).

Chapter XI

1. We in the Working Group would prefer a statutory Commission of the type envisaged by the Bhabha Committee in its Report in 1952. The political and economic changes over the last few years underscore the necessity for insulating the administration of the Companies Act and related matters from the pulls and pressures of conflicting political and economic idealogies, and the desirability of entrusting it to the care of an independent Commission or Authority, consisting of competent persons from industry, trade, administration, and the professions, on a full-time basis. The need for this would be greater, if, as we recommend in a following chapter of our report, the administration of the Companies Act is also placed in charge of the same Ministry in the Government of India, as may be dealing with the other related measures and enactments, like Capital Issue Control, Stock Exchange, Finance Corporations, etc.

If, however, Government do not consider it feasible to set up a high-power Statutory Commission or Authority which was recommended by the Bhabha Committee and which we still favour, there is no other alternative but to fall back on a full-fledged Secretariat Department which should make use of the services of experts from outside on a contract basis. (11.5).

2. We consider that it will be a major step towards streamlining the present organisation for the administration of the Companies Act and related matters at the top level, if the Company Law Board which has no longer any special functions to discharge is wound up and the responsibility for the administration of this Act is placed squarely and visibly on the Department of company Affairs. (11.8).

3. From the evidence that we received at all the leading centres of trade and industry, it was clear that the pattern of regional and State organisations was considered suitable and adequate for the enforcement of the Companies Act. We have no doubt that, with appropriate reinforcement of staff strength, the offices of the Registrars in the States would be able to cope with the additional work which they may be called upon to handle when the other related subjects like Capital Issue Control, Stock Exchange, Finance Corporations and the few other measures and enactments to which we refer in the following chapter, are also transferred to the Department responsible for the administration of the Companies Act, (11.10).

4. We recommend that the present northern region be bifurcated into two Directorates—one with its headquarters at Kanpur as at present and the other with its headquarters at Delhi. (11.12).

5. Our view is that such of the powers as affect the day-to-day work of companies and do not involve any major departure from the basic policies embodied in the Act or in well-established company practice, it would be an advantage alike to the Administration and to the business community to delegate them to the Regional Directors. For they would be able to deal with the local businessmen more conveniently than the Department of Company Affairs situated in New Delhi could do. In the light of our general view on this subject we suggest that a departmental committee under the Chairmanship of the Secretary of the Department of Company Affairs should go into this subject and prepare a scheme of further delegation of powers to the Regional Directors without delay. (11.15).

6. We recommend that some of the powers vested in the courts of law should also be advantageously transferred to the Regional Directors. We mention a few of them by way of illustration only:—

Section 17. Amendment of the Memorandum of Association of a company.

Section 17. (Subject to such guiding principles as the Department of Company Affairs might lay down).

Section 141. Rectification of the Register of charges and extension of time for registration.

Section 163 (vi) Order compelling immediate inspection of documents when refused.

Section 234-A. Sanction to the Registrar of Companies for seizure of company records. (On the lines of similar powers given to Collector of Customs under the Customs Act.)

Section 240-A. Sanction to Inspectors for seizure of records (Similar to powers given to the Collector of Customs under the Customs Act.)(11.16).

7. In regard to Sections 234A and 240A of the Act, the Department of Company Affairs may lay down detailed guidelines for the use of Regional Directors and further require that a short statement of cases should be sent to the Department before the necessary sanction to the Registrars and Inspectors is given. An amendment of the Act would be needed to give effect to our suggestion about the transfer of powers from the courts to the Regional Directors. This will provide to all those who are interested in or concerned with this subject with a reasonable opportunity for debating the issues of policy involved in our recommendation. (11.17).

8. If our recommendation for the unified administration of the Companies Act and other related subjects, to which we refer in Chapter XII of this report, and for the establishment of a comprehensive ministry at the Centre, dealing with all these subjects is accepted, we anticipate an appreciable addition to the load of work in the Office of Regional Directors and Registrars of Joint Stock Companies, particularly at the higher levels. These offices will in that event require not merely some quantitative addition to their staff strength but also a better calibre of personnel in their higher ranks. Further, if the Administrative responsibility for supervising the work of the Official Liquidators is to be increasingly transferred from the courts to the Regional Directors, this will also call for a sizeable strengthening of the staff strength in the regional offices of the requisite competence. This is a subject which has to be examined in some depth, on the basis of facts and figures and the relevant statistics relating to the existing staff strength in these offices. It is important that this study should be undertaken by a high power departmental committee under the Chairmanship of the Secretary of the Department as soon as a decision on the major policy issues raised by us has been taken. (11.18).

9. We fully endorse the observations of the Estimates Committee of Parliament contained in their 53rd Report, 1963-64, in which they commented on the excess fee-earning of the Department and suggested that as the amount of fees realised from the joint stock companies during the previous three years had far exceeded the amount of expenditure on the Administration of the Companies Act, the question of crediting the excess revenues to a special fund for the purpose of undertaking research in corporate matters and in imparting training to company accountants, company secretaries, etc., might be examined. The expenditure on the additional staff strength which we have suggested for the offices of the Regional Directors and the Registrars would be legitimate charge on the surplus of the fee-income earned by the Department. (11.18).

10. Closely allied to the question of staff strength is that of improving the quality of the officers and the senior staff not only in the Regional and the Registrars Offices but also at the headquarters of the Department of Company Affairs itself. If the Department and its regional and state offices are to be fully prepared for and geared to the additional responsibilities which we visualise for them, it is essential that arrangements for systematic periodical in-service training and orientation courses for the officers and staff of the Department should be made. (11.19).

11. At an earlier stage in the history of the Department of Company Affairs, a close link had been forged between the then Department of Company Law Administration and the Institutes of Management at Ahmedabad and Calcutta and the Staff College

at Hyderabad and some private commercial training institutes in Bombay and Madras. These links should be revived, and a continuing system of training and periodical orientation courses should be organised and programmed for. (11.20).

12. So far as the managerial personnel needed for Public Sector Undertakings is concerned, we consider that there is need for close collaboration between the Department of Company Affairs and the Bureau of Public Enterprises. (11.21).

13. If our recommendation for a comprehensive Central Ministry to deal with the Companies Act and all other related subjects is accepted by Government, the need for such collaboration would be inescapable. It is not enough that the Secretary or some other Senior Officer of the Department of Company Affairs is a member of the Coordinating Committee which functions as the governing body of the Bureau of Public Enterprises. It is also necessary that the work of the Bureau in regard to the recruitment, training and placing of managerial, legal and accounting personnel of companies is closely integrated with the activities of the Department of Company Affairs in this area. This Department is closely connected with the profession of the company lawyers and company accountants and also with the problems of management of companies and should be in a position to offer the necessary technical advice and guidance to the Bureau in the formulation of its plans and programmes in regard to the recruitment and training of specialised managerial personnel concerned with management. (11.22).

14. One aspect of the type of integration between the Bureau of Public Enterprises and the Department of Company Affairs which strikes us as being full of administrative potentialities is the better utilisation of the accounting, legal, financing and other experts who are now in the Company Law Board Service, not only in public enterprises but also in other branches of Administration. (11.22).

Chapter XII

1. We are convinced that there is a strong case for bringing all the related subjects, viz., capital issue control, stock exchange, financial corporations, including the Industrial Finance Corporation, the State Finance Corporations, the Industrial Credit and Investment Corporation of India, etc., and the profession of accountancy, under one administrative roof. The case is so overwhelming that any marginal advantages which now accrue to some of the other secretariat departments from the present haphazard distribution of subjects among them are more than offset by the serious damage caused to the administrative effectiveness of these measures by their fractionated administration in

different ministries. Government can never expect to produce any impact on the corporate sector if different governmental or quasi-governmental agencies continue to pull at each other and fail to evolve a coordinated and integrated policy under which alone the different types of administrative weapons in the departmental armouries of Government can be welded purposefully for the purpose of achieving the common objects and goals of all these agencies. (12.4).

2. While we do not feel called upon to pronounce on the claims of any of the existing Ministries to these subjects, we are convinced that in the interest of the efficient and purposive administration of not only the Companies Act but also of the other related enactments dealing with the Stock Exchanges, the Industrial Financial Corporations, the Life Insurance Corporation and the Unit Trust together with these institutions must be administered under the broad policy guidance of one and the same Ministry. (12.8).

3. We consider that the authorities of all financial and financing institutions should try to evolve a comprehensive and coherent policy as to their duties and responsibilities, as important shareholders in the large number of joint stock companies in which they invest their funds. (12.12).

4. We are clear in our mind that it would not be feasible for these Institutions to take the desired initiative in regard to all matters, relating to their rights and duties as investors, much less to evolve common and concerted policies, fitting into their operational methods and practices, unless all of them are brought under the administrative policy guidance of one and the same Ministry in the Government of India. We, therefore, strongly recommend that all these subjects and agencies should be brought under one administrative roof in the Central Secretariat without avoidable delay. (12.13).

5. When the integrated Ministry which we recommend has been set up, Government should also consider the desirability of transferring to it those provisions of the Industrial (Development and Regulation) Act which deal with the investigation of companies in distress. (12.14).

6. The laws which deal with the organisation, structure and management of other institutions, e.g., the provisions of the Banking Laws (Miscellaneous Provisions) Act relating to the management of commercial banks and banking institutions, should also be administered in close consultation and collaboration with this integrated Ministry, so that, as far as possible, uniform regulatory policies in regard to the structures and

functions of all joint stock companies may be evolved and unnecessary duplication or regulatory work in the different Ministries may be avoided. (12.15).

7. We suggest, that, pending consideration of this recommendation relating to a comprehensive view of the activities of the Financial Institutions, Government should forthwith initiate measures to provide for the maximum possible degree of consultation and co-ordination in the working of these institutions and agencies, in a more meaningful and purposive manner than they have been administered so far.

This can be best done by the establishment of inter-departmental standing committees both at the headquarters and the regional offices of these different institutions and agencies in all important commercial areas of this country, and to a limited extent by the inter-change of personnel among these institutions whenever opportunities for such inter-change arise. The duties and responsibilities of the suggested standing committees should be laid down with reasonable precision, and the heads of these institutions should be encouraged to associate with one another freely, as administrative experts and specialists, without being hindered by their departmental or ministerial attachments. (12.17).

Chapter XIII

1. If the Central Government is to guide Official Liquidators effectively in future and if winding up proceedings are to be expedited, it is necessary to strengthen the staff now attached to the offices of the Official Liquidators and to improve their quality. (13.6).

2. The law requires the preparation of a report by the Official Liquidator for submission to the Court, stating that the affairs of a company voluntarily wound up have not been conducted in a manner prejudicial to the interest of its members or to public interest. We recommend that the law on this subject be suitably amended to relieve the liquidators of this additional burden of work which they can hardly carry. In our view, this important work of an investigational nature should be undertaken by the Department through its regional and state organisations only in the case of public companies, and also of these public companies which have been converted into private companies. (13.9).

3. We consider the present administrative arrangement regarding internal audit teams for liquidation matters to be salutary and desirable, but would suggest that the Audit Officer for each region should be a person of sufficient seniority and standing to be able to discuss matters on an equal footing with the Official Liquidator. We trust the Official Liquidators would also look

upon the Audit Officers as their colleagues in a common task, and not as outsiders imposed on them. We also suggest that instead of one unit for the Southern and Northern regions combined, separate units for every region should be provided in the interest of administrative efficiency. (13.11).

4. Certain powers in respect of liquidation proceedings which are now exercised by the High Courts in Chamber could, without much damage to the basic principles underlying these provisions be transferred to the Central Government. (13.14).

5. We would recommend that all other powers relating to the winding up of companies should be exercised by the Company Tribunals which we propose should be set up in the principal administrative regions of this country. (13.15).

Chapter IV

1. We are convinced that it is most desirable that administrative tribunals should be set up at least in the more important commercial centres of this country, and that an appellate administrative tribunal with some limited original jurisdiction, might with advantage be set up at the seat of the Central Government to handle and dispose of the increasingly large number of company cases which are now referred to the courts of law. The jurisdiction of these administrative tribunals might also include adjudication of cases falling under other Acts which are directly or indirectly concerned with the working of the corporate sector. (14.8).

2. In the light of our thinking on the subject and the evidence that we received from many quarters, we are clear in our mind that the reasons for the failure of the first Companies Tribunal to realise the expectations of its sponsors do not in themselves rule out the case for the setting up of a properly constituted administrative Tribunal with Branches situated at the various Regions to which the powers of the court conferred under the various Section of the Companies Act, could be transferred for final disposal, with a provision for appeal to an Appellate Administrative Tribunal at Delhi on questions of fact and law, and in special cases, a further appeal to the Supreme Court only on fact that only a highly selective membership of the Tribunal reflecting the type of varied competence needed for dealing with complicated business issues, aided by a carefully workedout procedure could be expected to ensure the successful working of any Tribunal. Unless these conditions are fulfilled, we see litttle possibility of any such Tribunal producing the results expected of it. (14.15).

3. We trust that our suggestion for an in-built alternative remedy by way of appeal to an Appellate Administrative Tribunal at the Centre, and for a further appeal on questions of law to the Supreme Court of India will be found to be in accordance with the accepted cannons of limitation on the exercise of the prerogative writ jurisdiction and the High Courts will not be called upon to interfere in company cases in exercise of their extraordinary powers. (14.16).

Chapter XV

1. While it is clear that several provisions of the Companies Act cannot be usefully applied to Government companies as defined under the Act, our general view is that the Act should apply to Government companies in the same way as it applies to the non-government companies; otherwise, the already existing incipient feeling in business circles that there is undue discrimination in favour of Government companies will further grow. (15.3).

2. If the management of Government companies or the administrative departments dealing with them consider that certain specific provisions of the Companies Act should not apply to them, it should be for them to make out a case for exemption of such Government companies from those provisions. Section 620 of the Companies Act enables the Central Government to modify the Act in relation to government companies in the manner indicated in that Section. One of the requirements of this Section is that copies of the necessary notifications exempting government companies from the provisions of the Act must have the approval of the two Houses of Parliament. We think this is a salutary requirement and government companies should have no difficulty in complying with this procedure. (15.3).

3. We were told that neither in the formative nor in the operative stages of government companies did the administrative department of such companies maintain as close contacts as they might be expected to have with the Department in charge of the administration of the Companies Act. If our recommendation about the need for close co-ordination of work between the Bureau of Public Enterprises and the Department of Company Affairs is accepted, this, we hope, will ensure much closer co-ordination between government companies and the Department concerned with the administration of the Companies Act. (15.4)

4. An important point made by some witnesses to ensure quick disposal of cases was that suitable target dates should be fixed for this purpose. We understand that detailed time-schedules have been laid down for the processing of cases under

different sections of the Act and for their final disposal within the time limits set in the schedules. In this connection we recommend that—

(a) these time-schedules for different classes of cases should be widely made known to the business community;

(b) the Under-Secretaries and Deputy Secretaries concerned should keep a close watch on the observance of the target dates prescribed;

(c) in all cases of appreciable deviation from the targets, they should be brought to the notice of the Joint Secretaries and the Secretary of the Department, depending on their importance;

(d) suitable administrative action on undue delays in the disposal of cases should be taken against the officers and staff concerned; and lastly

(e) in the Annual Report on the Administration and Working of the Companies Act for the previous year, a list of cases where there has been a substantial deviation from the target dates fixed for them should be conveniently reproduced. (15.5)

5. It was suggested to us that a uniform accounting year should be prescribed for all companies. We consider that the time has now come when companies should be required to fall in line with this suggestion from such suitable future date as Government may prescribe in consultation with the industrial and commercial associations. A beginning towards this end may be made by requiring at least all companies falling under the same industrial classification to conform to one uniform accounting year. In the second stage of progress, the same accounting year for all companies could be fixed from a convenient future date, may be within two years from now. (15.6)

6. It was suggested to us by Shareholders Associations and by several spokesman of the Stock-Exchange that public companies listed on the Exchanges should be required to publish at least half-yearly reports on their work and accounts, if not quarterly. We have little doubt that this will help to encourage investments in company shares and debentures. We would also recommend a simplified version of the accounts to be devised in consultation with the profession of accountancy to be made available along with the half-yearly reports, leaving the details to be provided along with the annual reports as at present. (15.6)

7. We consider it essential that all 'diversified' public companies should be required to prepare separate accounts for

the different lines of business carried on by them, so that the performance of the different units in such companies may be known and made available on request to shareholders and to Registrars of Joint Stock Companies. (15.6)

8. We consider that it is very desirable that the Directors' Reports for 'diversified' companies should invariably include brief accounts of the performance of the different units in such companies so that their actual performance and their problems and difficulties, if any, may be made known to their shareholders. (15.6).

9. As regards the accounts of group companies, we recommend that a consolidated statement of the accounts of all companies within a group should be prepared. Such companies should not thereafter be required to attach the accounts of its subsidiaries along with its own accounts. It should, however, be open to any shareholder of the holding company to ask for the accounts of any or of all the subsidiary companies and it should be the duty of the holding company to make these documents available to such shareholder. (15.6)

10. We accept the suggestion of the Controller of Capital Issues that the Reserve Bank should not specifically issue a permit to any foreign company to establish a place of business before any such company is registered in this country. We also recommend that the adequacy of the provisions of the Companies Act, 1956, in Part XI should be examined afresh in order to consider how more effective supervision could be exercised over the activities of foreign companies operating in India. (15.7)

11. It has been brought to our notice that many foreign companies working in India are foreign only to the extent of their place of incorporation; there is nothing in the Companies Act, 1956 which could ensure that the business of these companies is carried on in conformity with the basic principles underlying our Company Law. In our view, therefore, this problem relating to foreign companies of this type needs to be re-examined urgently against the background of our general economic policy relating to the role of foreign business and investments in India. (15.7)

12. In particular, having regard to the necessity, increasingly brought home to us in recent months by the exigencies of our current and foreseeable foreign exchange budgetary position, for an objective balancing of the benefits and costs of foreign participation in joint ventures, we feel that an important object

of our future policy in this area should be to safeguard the position and powers of the Indian partners in joint venture and to ensure that their status and authority as the 'management on the spot' are not undermined. For this purpose we would suggest that suitable provisions in the Companies Act, 1956, may be incorporated on the analogy of the provisions of Section 409 of the Act to ensure that the control oved the management of joint venture by their Indian partners is not affected in consequence of changes in shareholding brough about merely as a result of market operations. (15.8)

13. Several shareholders' associations claimed before us that it was time that Government 'recognised' them in the same way as Government had recognised the stock exchanges. We the in sympathy with this demand and consider that Government should initiate a system of recognition, atfer consultation with the leading shareholders' associations in Calcutta. Madras and Bombay. (15.9)

14. In view of the few cases of the alleged issue of forged shares which have come to our notice, we would, strongly urge that suitable provisions should be made in the Companies Act to facilitate quick adjudication of conflicting claims of shareholders of the companies concerned, so that the interests of the companies do not suffer and they may not needlessly become involved in prolonged litigation resulting in liabilities which may financially cripple them. (15.12)

15. It is clear to us that some summary procedures for dealing with such tangled webs of claims and counter-claims in cases of this type must be devised within the frome-work of our company law. We, therefore, recommend that Section 155 of the Companies Act, 1956 should be suitably amended and elaborated to enable an appropriate authority to settle such disputes finally. If our recommendation for the establishment of a Tribunal for dealing with company cases is accepted, a matter of this type must necessarily be referred to this body. (15.14)

16. The detailed procedure to be followed by the company management for the issue of share certificates has also been laid down in the Companies (Issue of Share Certificates) Rules, 1960 which provides reasonable safeguards against the issue of spusions duplicate shares. Nevertheless, there is need for adjudication of the conflicting claims in those cases where disputes arise as to the authenticity of sharescrips. For this latter purpose, some special amendment of the provisions of the Companies Act is needed. For the reasons which we have already mentioned, we do not think any special legislation is necessary, as we consider that the scope of section 155 of the Companies Act is wide enough to offer

sufficient jurisdiction to a court of law or to a Company Tribunal to adjudicate on the type of issues of conflicting rights and claims which we have discussed. (15.15)

17. **We recommend that the Reserve Bank of India should examine the feasibility of requiring scheduled banks which advance loans exceeding, say, Rupees 5 lakhs to any one borrower, against shares, to furnish the essential particulars to the Reserve Bank of the scrips pledged with them. (15.16)**

9197 P&S—Govt. Press, Chandigarh.